S. Hrg. 99-785

THE RAILROAD ANTIMONOPOLY ACT OF 1985

HEARINGS

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST AND SECOND SESSIONS

ON

S. 447

A BILL TO AMEND THE SHERMAN ACT TO PROHIBIT A RAIL CARRIER FROM DENYING TO SHIPPERS OF CERTAIN COMMODITIES, WITH INTENT TO MONOPOLIZE, USE OF ITS TRACK WHICH AFFORDS THE SOLE ACCESS BY RAIL TO SUCH SHIPPERS TO REACH THE TRACK OF A COMPETING RAILROAD OR THE DESTINATION OF SHIPMENT AND TO APPLY CLAYTON ACT PENALTIES TO MONOPOLIZING BY RAIL CARRIERS

APRIL 23, SEPTEMBER 24, 1985; AND MARCH 4, 1986
WASHINGTON, DC

AUGUST 29, 1985
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THE RAILROAD ANTIMONOPOLY ACT OF 1985
S. 447

TUESDAY, APRIL 23, 1985

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met at 10 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Strom Thurmond (chairman of the committee) presiding.

Also present: Senators McConnell and Denton.

Staff present: Kenneth Starling, Cynthia Lebow, Nick Chumbris, Robert Feidler, Bill Sims, and Victor Maddox.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The CHAIRMAN. Today we will hear testimony on S. 447, a bill introduced by Senator DeConcini, who is a distinguished member of our committee. Senator DeConcini's bill, entitled the "Railroad Antimonopoly Act of 1985," is intended to address a situation faced by some shippers of bulk commodities on railroads. The shippers in question are usually located on or near the tracks of only one railroad and are thus captive to that railroad in the sense that they do not have ready access to competing carriers.

With deregulation of the railroads, following passage of the Staggers Act in 1980, railroads have certain flexibility in setting their prices to shippers. The railroads may charge different prices to shippers in different markets, in response to the degree of competition faced by the railroad in each market. This differential pricing flexibility was an intended result of railroad deregulation.

In this hearing, we will hear testimony on whether the current antitrust law against monopolistic pricing, and the protections provided to captive shippers in the Staggers Act, are adequate. The question before us is whether there is a need for an additional explicit provision in the Sherman Antitrust Act to guard against monopolistic treatment of captive shippers.

Senator DeConcini has broken his ankle and will not be able to be here and, without objection, I will at this time place his opening statement in the record following mine.

[Prepared statement of Senator DeConcini follows, along with the text of his bill S. 447:]

OPENING STATEMENT OF SENATOR DENNIS DECONCINI

Mr. Chairman, I appreciate your scheduling this hearing in such timely fashion. The issue of the scope of application of the antitrust laws to the rail industry is one of growing importance and concern and was highlighted recently by the antitrust issues surrounding the Conrail sale.

It becomes an even greater issue when we consider the shrinking number of major railroads that now control the bulk of the trackage. In addition to the Conrail sale, I am following with interest the pending merger of the Southern Pacific and Santa Fe. This merger will reduce to one the number of major railroads serving my home State and the Southwest. By the end of the year it is probable that there will be only five major rail systems in the country. With this concentration of power comes the opportunity to engage in practices that will lessen competition and be monopolistic.

It is my hope that the extension of the antitrust laws to the rail industry will have a healthy influence on promoting competition in that industry. I have supported the process of deregulation of the railroads that began in the mid-seventies and culminated with the passage of the Staggers Act five years ago. But with regulation largely removed a void has been created that has left many shippers remediless in dealing with practices of railroads that might be against the public interest and which suggest an abuse of a monopolistic power. I believe that application of the antitrust law to railroads would fill this void and is the logical next stop in the deregulatory process.

I am pleased that Senators Simpson, Andrews and Nickles have cosponsored S. 447. On the House side, Congressman Seiberling has sponsored an identical bill which has drawn a large number of Democratic cosponsors and which will soon be the subject of hearings. This bipartisan support from around the country emphasizes the broad spectrum of interests that have a real stake in assuring that the rail industry is driven by forces of competition.

Since the introduction of the bill in February, I have met with many interested parties to review the principles of S. 447 and its technical aspects. Many good suggestions have been forthcoming, and I am seriously considering adopting a number of changes to the bill that will tend to make it more of a "pure" antitrust bill. For example, should the remedies of the bill be limited to bulk commodity shippers? What legal test should be applied in determining if an illegal act has occurred? Are certain sections of the bill that smack of reregulation proper? I have an open mind on these and other issues.

I look forward to hearing from our distinguished panel of witnesses and exploring these issues with them.

99TH CONGRESS
1ST SESSION

S. 447

To amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment and to apply Clayton Act penalties to monopolizing by rail carriers.

IN THE SENATE OF THE UNITED STATES

FEBRUARY 7 (legislative day, JANUARY 21), 1985

Mr. DECONCINI introduced the following bill; which was read twice and referred to the Committee on the Judiciary

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A BILL

To amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment and to apply Clayton Act penalties to monopolizing by rail carriers.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Railroad Antimonopoly Act of 1985".

SEC. 2. (a) The Congress finds that railroad rates and terms of service are best and most efficiently established in a competitive marketplace.

(b) The Congress finds that in many instances a competitive marketplace does not exist because of conditions such as those described below:

(1) The source of supply of a bulk commodity is served by a single rail carrier that has exclusive control of the railroad facilities from the source of supply to a point of interconnection with another rail carrier. Beyond such point of interconnection alternative rail routes exist to the destination to which the commodity is shipped, and such routes would be competitive were it not for the monopoly of the originating carrier over the movement from the source of supply to the point of interconnection. The originating rail carrier uses its monopoly to eliminate competition over the entire route and to assess charges or require other terms of service less favorable than those that would be assessed or required in a competitive environment for the movement over its track or railroad facilities from the source of supply to the point of interconnection.

(2) A similar situation exists where a delivering or connecting rail carrier has exclusive control of tracks or railroad facilities which give it a monopoly from a

point of interconnection with another carrier to the destination of the movement or to a second point of interconnection with another carrier.

(3) Situations also addressed by this Act exist where a rail carrier has exclusive control over track or railroad facilities and monopolizes movements within the area of its exclusive control, or where two or more rail carriers have joint or mutual exclusive control over track or railroad facilities and so monopolize its use.

(c) The purposes of this Act are to restore, establish, or enhance competition by eliminating the ability of the originating, connecting, or delivering carrier, as the case may be, to assess charges or to require other terms less favorable than those that would be assessed or required in a truly competitive environment.

SEC. 3. The Sherman Act (15 U.S.C. 1) is amended by adding after section 8 the following new section:

"SEC. 9. (a)(1) It shall be unlawful for an owner rail carrier to monopolize or attempt to monopolize by denying or threatening to deny to any shipper or another rail carrier the use on reasonable terms of a railroad facility which is the sole facility over which such shipper can move bulk commodities by rail to connect with the track of a competing rail carrier or to reach the destination of shipment.

"(2) A violation of paragraph (1) shall not occur where an owner rail carrier permits, on reasonable terms determined in accordance with generally accepted principles regarding just and reasonable rental of track, another rail carrier offering competing service to use such sole railroad facility. If the owner rail carrier permits such use of the sole railroad facility by a rail carrier and resulting bona fide competition exists for the transportation of the shipper's goods, the carrier transporting shippers commodities shall not be restricted in its rates by any provision of this Act.

"(3) If the owner rail carrier does not offer use of its tracks to a competing rail carrier, as provided in paragraph (2), or if no competition materializes from any competing rail carrier, the owner rail carrier shall offer rates to a shipper for transportation of its bulk commodities over the sole railroad facility at rates which are no higher than would yield a fair return on the proportion of the owner rail carrier's prudent investment in the sole railroad facility that the shipper's traffic bears to all traffic using such sole railroad facility.

"(b) It is unlawful for the owner rail carrier—

"(1) to condition the use of the sole railroad facility upon use of other facilities of the owner rail carrier, or

"(2) to suspend or threaten to suspend service over the sole railroad facility by reason of a shipper's asserting its rights under this section.

"(c) If connection with a water carrier exists at or within reasonable proximity of the first connection with a competing rail carrier, the shipper may elect to connect with the water carrier instead of or in addition to connecting with a competing rail carrier; provided that the cost of interconnection is no greater than would be occasioned by interconnection with the first competing rail carrier, or the owner rail carrier is reimbursed for the difference in cost.

"(d)(1) Any person injured in his business or property by reason of a violation of subsection (b) of this Act may bring an action therefor in accordance with the provisions of section 4 of the Clayton Act.

"(2) Any person shall be entitled to sue for and have injunctive relief as provided in section 16 of the Clayton Act for threatened loss or damage by reason of a violation of this section, notwithstanding any limitation contained in the proviso of such section 16 of the Clayton Act.

"(e) For purposes of this section the term—

"(1) 'rail carrier' means a person or persons providing for compensation railroad transportation in or affecting commerce;

"(2) 'owner rail carrier' means the rail carrier which owns or controls exclusively or jointly a sole railroad facility;

"(3) 'railroad facility' includes all facilities commonly included in the term 'railroad' which are necessary or practical for the movement of commodities over the sole railroad facility;

"(4) 'sole railroad facility' means a railroad facility which is the only facility by which a shipper can move bulk commodities by rail to connect with a competing railroad. Use of the sole facility 'to the destination of shipment' does not include use of railroad facilities beyond the point of connection or points of interconnection;

"(5) 'shipper' includes—

"(A) a person engaged in a business other than transportation who, in furtherance of such business, moves its own goods or arranges for transportation of commodities which it has sold; and

"(B) a person engaged in intermodal transportation who is a purchaser of rail service used in such intermodal transportation commonly called a 'shipper's agent';

"(6) 'bulk commodities' includes bulk goods moved in carload lots, such as coal, ore, grain, fertilizer, dry chemicals, primary forest or wood raw materials, and perishable commodities for human consumption when shipped in service which includes ToFC service;

"(7) 'primary forest or wood raw materials' includes logs, pulp wood, dressed or treated poles and saw mill or planing mill products;

"(8) 'service which includes ToFC service' means service to a shipper who customarily uses transportation by rail or trailers on flat cars (ToFC service) as a part of any given shipment, but does not exclude service to such shipper of some shipment by rail not employing ToFC service;

"(9) 'dry chemicals' means substances identifiable by chemical formulae and commonly described as chemicals, such as soda ash, silica gel, caustic soda, and sodium sulfate;

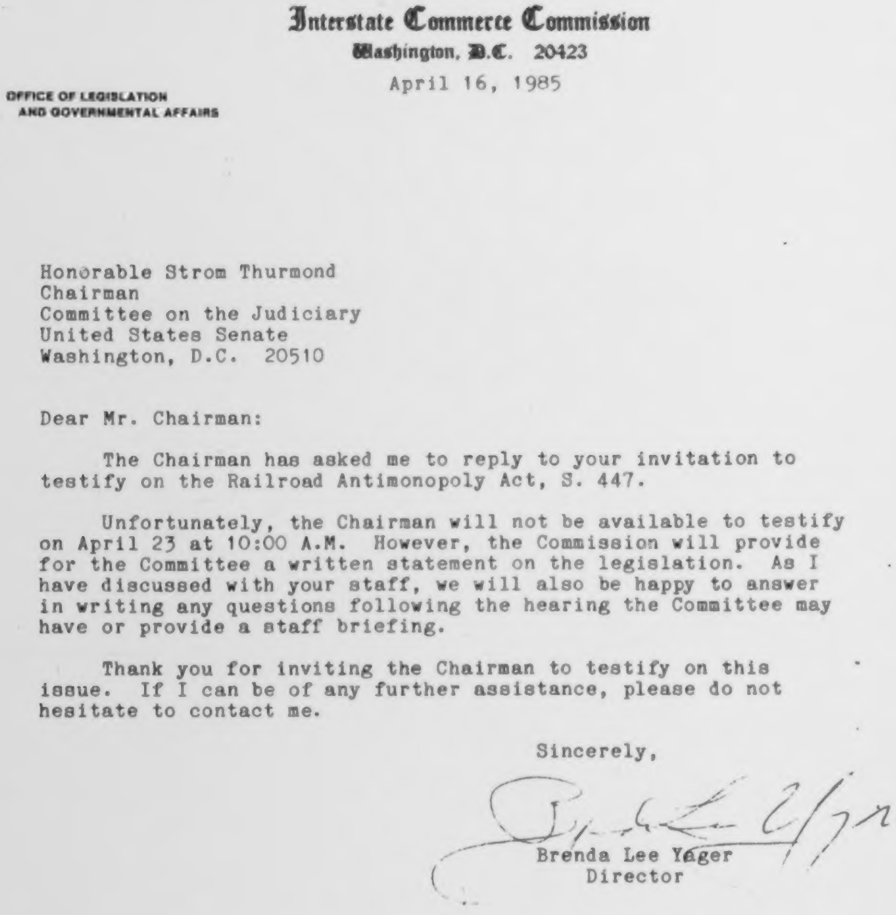
"(10) 'track of the competing rail carrier' means track subject to the competing carrier's use but does not include tracks jointly used by the rail carrier denying use of the sole facility; and

"(11) 'connect' includes connection from the point of origin, point of destination, and/or point of interconnection with another carrier.".

○

The **Chairman**. We welcome our distinguished witnesses today and look forward to their testimony. I note that the Chairman of the Interstate Commerce Commission was invited to attend but was unable to be with us today. Instead he is submitting a statement for the record.

[Statement follows:]



Interstate Commerce Commission
Washington, D.C. 20423

OFFICE OF LEGISLATION
AND GOVERNMENTAL AFFAIRS

April 16, 1985

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

The Chairman has asked me to reply to your invitation to testify on the Railroad Antimonopoly Act, S. 447.

Unfortunately, the Chairman will not be available to testify on April 23 at 10:00 A.M. However, the Commission will provide for the Committee a written statement on the legislation. As I have discussed with your staff, we will also be happy to answer in writing any questions following the hearing the Committee may have or provide a staff briefing.

Thank you for inviting the Chairman to testify on this issue. If I can be of any further assistance, please do not hesitate to contact me.

Sincerely,

Brenda Lee Yager
Director

STATEMENT OF REESE H. TAYLOR, JR., CHAIRMAN
INTERSTATE COMMERCE COMMISSION
BEFORE THE SENATE COMMITTEE ON
THE JUDICIARY ON S. 447

April 23, 1985

Mr. Chairman and Members of the Committee:

I want to thank you for this opportunity to submit the views of the Commission on S. 447, a bill "to amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment and to apply Clayton Act penalties to monopolizing by rail carriers."

The stated goal of the bill, which is similar to S. 2417, introduced in the last Congress, is to foster competition in the rail industry and to bring fair treatment to captive shippers, by placing the rail industry within the scope of the antitrust laws. It seeks to enhance competition in areas now served by only one railroad in an effort to insure the benefits of competitive prices to consumers and the shippers that serve them.

S. 447 attempts to achieve this goal by making it unlawful for a rail carrier to monopolize or attempt to monopolize, by denying, or threatening to deny, to any shipper or another rail carrier the use, on reasonable terms, of a railroad facility which is the sole facility providing rail services to a shipper of bulk commodities. If an "owner" rail carrier serving such a shipper permits another carrier to serve the shipper over its lines for reasonable track rental charges, the owner carrier is not in violation of the Sherman Act. If another carrier, in fact, does provide service over the owner railroad's lines, and bona fide competition thus exists, the bill would not restrict the rates assessed. However, if the owner carrier does not offer trackage rights for reasonable charges, or if it does so offer but intramodal competition does not "materialize", the bill would limit the rates that could be charged.

Thus, if an owner carrier only offers trackage rights at unreasonable charges, it apparently would be in violation of the Sherman Act and would also be limited in the rates it could offer. Also, it appears that even if an owner carrier offers reasonable trackage rights arrangements and, therefore, is not in violation of the antitrust laws, but, for whatever reason, no competing carrier accepts those arrangements, the owner carrier is nonetheless limited in the rates it can assess.

The bill also provides that it is unlawful for the owner rail carrier: (1) to condition the use of the sole facility upon use of other facilities of the owner rail carrier; or, (2) to suspend or threaten to suspend service over the sole railroad facility because a shipper has asserted its rights under this legislation. Additionally, the bill includes a provision which allows a captive shipper to use the lines of an owner railroad to connect with a water carrier, if the water carrier is within reasonable proximity of the rail connection. Finally, the bill provides for certain remedies set forth in the Clayton Act.

In essence, S. 447 attempts to restrain rail rates for "captive" shippers by requiring a rail carrier to allow trackage rights over its lines to another carrier in order to permit that carrier access to the shipper. If the owner carrier denies use of its facilities on "reasonable" terms to such a shipper or another rail carrier, the owner carrier would be in violation of the Sherman Act, and would also be limited in the rates it could charge.

The Staggers Act was intended to assist the rail system to remain viable in the private sector and to allow the railroads to compete more effectively among themselves and with other modes of transportation. While there is greater reliance on the forces of the marketplace, a regulatory process remains to balance the needs of carriers, shippers and the public where warranted, such as in the absence of effective competition.

We believe, and have so testified before this Committee, the Senate Commerce Committee and the House Committee on Energy and Commerce, that, in general, the Staggers Rail Act is working well. In our view, the Act and our implementation of it have been successful in removing unnecessary regulation, encouraging efficient carriers to earn adequate revenues, and balancing the interests of the parties in accordance with the goals of the Act. Many of the provisions of the Staggers Act, such as the provision authorizing and encouraging the use of contracts and the provision restricting rate bureau activities, have resulted in more effective competition among rail carriers and with other modes. We recognize, however, that certain changes in railroad policy and operations have been unpopular. One of those changes has been in the area of reciprocal switching, one method of alternative access. The Staggers Act prompted rail carriers to review existing arrangements and to limit some of these arrangements to reflect existing competitive conditions and revenue need.

This is a major area of concern to which S. 447 is directed. But S. 447 would go further and, given the possibility of Sherman or Clayton Act prosecution, would have the effect of requiring trackage rights on any part of a carrier's system rather than being limited, as is 49 U.S.C. §11103, to reciprocal switching arrangements in terminal areas. As a result, this bill presents a number of practical problems. We are also concerned that it does not reflect the basic economic policies of the Staggers Act and the balance that was intended in that Act. Finally, we believe the proposed bill will create competing regulatory systems, one administered by the ICC and the other through the court system. The conflict between the two appears irreconcilable.

The bill does not address certain legitimate operational concerns. 49 U.S.C. 11103 recognizes that alternative access must be "practicable" and must not impair the primary carrier's use of its facilities. This is a complex question of fact. Authorizing access should not be permitted to cause inefficient operations by either or both carriers. The bill further complicates matters by authorizing shipper operation of the carrier's rail equipment. There are also implications for labor (if traffic is diverted) and questions of liability for accidents or misuse by shippers or another rail carrier.

There is no limit to the distance for which trackage rights would be available in theory for captive shippers of bulk commodities. If this is not addressed, the bill could have the effect of creating a nationalized trackage system for these commodities and artificially control prices for track rental. We also note that Section 3(2) uses the term "generally accepted principles" apparently referring to trackage rights compensation. There are no such principles, and the ones utilized in the *Union Pacific* merger[1] or in the *Frisco* formula[2] were unique formulae designed for unique situations. Therefore, there may be a question as to what the statute means.

Also, the bill would not allow consideration of competitive circumstances in determining the price for track rental or the rates to be charged if no bona fide competition results from reasonable charges for trackage rights. The bill's use of

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[1] See *Union Pacific--Control--Missouri Pacific; Western Pacific,* 366 I.C.C. 458, 589-90 (1982), *aff'd sub nom. Southern Pacific Transp. Co.* v. *ICC*, 736 F.2d 708 (D.C. Cir. 1984), *cert. denied sub nom. Kansas City Southern Ry. Co.* v. *United States,* Nos. 84-621, *et al.* (U.S. Feb. 19, 1985) (Commission decision leaving negotiation of trackage rights compensation to the parties unless they could not reach agreement, in which case they could petition the Commission to set trackage rights compensation); *Union Pacific--Control--Missouri Pacific; Western Pacific,* 1 I.C.C.2d ____ (1984) (decision setting compensation for trackage rights on petition by the parties).

[2] *St. Louis-S.F. Ry. Co.--Compensation--Chicago, R.T.&P.,* 363 I.C.C. 248 (1980), *aff'd sub nom. Gibbons* v. *United States*, 660 F.2d 225 (7th Cir. 1981).

"reasonable terms" does not allow any consideration of demand elasticity, differential pricing, or revenue need. Rail carriers must be permitted to price services efficiently and with reference to a particular situation if they are to be profitable in the private sector. The bill prohibits them from doing so, and, instead, establishes an artificial rate standard bearing no relation either to the individual movement or to the carrier's overall revenue need.[3]

The Staggers Act of 1980 created a regime of rate regulation for captive shippers. While carriers may adjust their rates freely where there is no 'market dominance', captive traffic is still regulated as to rates. It is a settled principle that where alternative intramodal competition exists, there is no market dominance and, therefore, no rate regulation. S. 447, by creating the potential for alternative intramodal routings in nearly all pertinent situations, would repeal by implication the ratemaking sections of the Staggers Rail Act. While the Commission could legally continue to consider maximum rate complaints, the likelihood of such regulation would be diminished sharply. This is so because the treble damage provisions of the Clayton Act, made available by S. 447 to trackage rights situations, would rapidly evaporate the Commission's utility. The trebling of damages will make carriers very reluctant to pursue efficient policies if there is any opposition. At the same time, the potential of gain through the capture of treble damages will become an incentive to use the courts to litigate even marginal problems that might otherwise be settled amicably. In short, marketplace rationality will be distorted from the perspective of both potential plaintiffs and potential defendants. The marketplace will become more legally contentious and the locus of the dispute will move away from the Commission, in the direction of forum shopping in the federal courts.

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[3] Section 3 also establishes the extremely complex task of determining what a railroad's "prudent investment" is. More specific guidelines would certainly be needed to minimize litigation in this area.

Finally, this legislation does not specify who is to make the various determinations, such as "prudent investments" for establishing rates under certain circumstances, required by the legislation. While the Staggers Act accords the railroads substantial rate freedom, to the extent rates remain subject to review, the Commission has exclusive jurisdiction to determine the reasonableness of rates and charges of rail carriers subject to ICC jurisdiction. S. 447 would have a significant impact on matters that are within the Commission's jurisdiction. For example, Section 3(3) appears to implement legislatively a modified form of stand-alone costing for rates charged on a rail line's monopoly segment where no alternate rail carrier appears to provide competition. The Commission is considering this issue in No. 347 (Sub-No. 1), Coal Rate Guidelines.

We hope these comments point out the complex questions that must be answered before rail carriers are required to allow competitors to operate over their lines (or risk Sherman Act prosecution). We are concerned that S. 447 fails to take into account these matters. As far as terminal-related access, we believe present §11103 is a preferable vehicle and we have used it to authorize alternate service where it is practicable and necessary to provide competition or is in the public interest.[4] Trackage rights on any part of a carrier's system, as provided by S. 447, is far broader and has great potential impact. It is an idea that we believe needs considerably more study prior to any action being taken.

Having concluded our comments on the bill itself, I would like to call to the Committee's attention a recently instituted proceeding which specifically addresses the matter of competitive access, the subject of S. 447. In a decision served March 28th of this year, the Commission announced its intention to adopt rules governing its handling of various competitive access issues, such as joint rates and through routes, reciprocal switching and terminal trackage rights.[5]

The institution of the proceeding is based on petitions filed by the National Industrial Transportation League and the Association of American Railroads, seeking our adoption of the competitive access rules which they have developed through lengthy negotiations.[6] Subsequently, Railroads Against Monopoly also submitted rules for adoption. The Commission is seeking comments on these proposals. Comments are due by May 17th and replies are due by June 3rd. Ultimately, the Commission will adopt rules which are consistent with statutory requirements and which are acceptable to as broad a section of the marketplace as is possible.[7] In our opinion, Ex Parte No. 445 (Sub-No. 1) is a more appropriate vehicle for the establishment of competitive access standards than the legislatively crafted solution in S. 447, particularly in view of the fact that we believe the bill leaves unresolved a number of serious legal and practical problems.

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[4] See Delaware & H. Ry. Co. v. Consolidated Rail Corp. 367 I.C.C. 718 (1983). This case demonstrates how complex this area is and the countervailing interests that must be balanced.

[5] Ex Parte No. 445 (Sub-No. 1), Intramodal Rail Competition, copy attached.

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SEPARATE EXPRESSION OF COMMISSIONER J.J. SIMMONS III:

Initially, I wish to disassociate myself from the confrontational tone adopted in portions of these comments. I also note that only Congress can ultimately determine whether the Commission's implementation of the Staggers Act has made new legislation necessary. However, I agree with my colleagues that Ex Parte No. 445 (Sub-No. 1) provides a useful forum for the Commission to reexamine the area of competitive access. It is possible that this proceeding may lead to resolution of some, if not all, of the concerns addressed in S. 447.

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[6] Petitioners were party to Ex Parte No. 456, The Staggers Rail Act of 1980-Conference of Interested Parties, decided September 10, 1984, which was instituted to gather information from carriers and shippers about the problems and benefits arising from the Staggers Act and to provide a forum for direct discussion among shippers and carriers. One of the areas considered in that proceeding was "competitive access".

[7] The Commission is handling this proceeding on an expedited basis, subject to the severe budgetary constraints the agency is currently experiencing.

EC

SERVICE DATE
MAR 28 1985

INTERSTATE COMMERCE COMMISSION

DECISION

Ex Parte No. 445 (Sub-No. 1)

INTRAMODAL RAIL COMPETITION

Decided: March 22, 1985

The Commission intends to adopt rules to govern its handling of various competitive access issues.[1] In this proceeding the Commission is inviting comment on the form these rules should take and whether the agreement reached by the National Industrial Transportation League and the Association of American Railroads and/or the proposal of Railroads Against Monopoly should be adopted.

On January 23 and 24, 1985, the National Industrial Transportation League (NITL) and the Association of American Railroads (AAR) filed petitions requesting us to adopt rules they have developed which would provide standards to govern the cancellation of through routes and joint rates, and the prescription of through routes, through rates, and reciprocal switching.[2] These rules are the product of lengthy negotiations that were initiated following denial of the NITL's initial petition. AAR and NITL state that the Commission has long encouraged parties to develop their own solutions, and that the agreement, while not resolving all the issues, represents a good faith effort to accommodate the legitimate interests of both shippers and railroads. They ask that the Commission publish a Notice of Proposed Rulemaking incorporating rules based on their agreement and soliciting comments. In addition, several other parties, including Consolidated Rail Corporation (Conrail), Union Pacific System, and the American Petroleum Institute, have filed pleadings which generally support the objectives of the agreement with certain reservations. These pleadings will be treated as comments and will be considered along with others received as a result of this notice.[3]

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[1] Competitive access is the term now in use to describe a number of intrarailroad operating practices, *viz.*, joint rates and through routes, reciprocal switching, and terminal trackage rights.

[2] The lead proceeding began in February 1983 when the NITL filed a petition to begin a rulemaking relating to rail rate changes, route restrictions, and terminal operations. In Ex Parte No. 445, *Standards for Intramodal Rail Competition* (not printed), served July 7, 1983, the Commission denied that petition. Among other reasons, we noted that no rules had been suggested. NITL and PPG Industries have petitioned to reopen that decision. In view of the action here, those petitions are now moot. NITL also petitioned for administrative review and reconsideration. Those petitions are denied.

[3] In Ex Parte No. 456, *The Staggers Rail Act of 1980 - Conference of Interested Parties*, decided September 10, 1984, the Commission instituted a proceeding to (1) gather information from carriers and shippers about the problems and benefits arising from the Staggers Act, and (2) provide a forum for direct discussion among shippers and carriers. One of the areas considered in that proceeding was "competitive access," which included joint rates, through routes, reciprocal switching, joint terminal service, and trackage rights. To the extent relevant, we will also incorporate into this proceeding the record that was developed in Ex Parte No. 456 and certified to the Commission on February 15, 1985.

On February 26, 1985, Railroads Against Monopoly (RAM)[4] submitted rules it proposes we adopt. In addition to the subjects covered in the NITL/AAR agreement, this proposal also covers terminal trackage rights. Conrail has filed a response to the RAM proposal. This pleading will be considered as a comment in this proceeding.

PRELIMINARY MATTERS

NITL has requested that its agreement with the AAR be adopted as interim rules during the period of notice and comment, and pending the development of final rules. Adoption of interim rules is, we believe, prohibited by the Administrative Procedure Act.[5] NITL does not offer a legal basis for interim rules and it appears that none of the exceptions to the APA notice and comment requirements are met here.[6]

THE PROPOSALS

NITL states that its proposed rules are necessary to maintain and promote the intramodal rail competition contemplated under the Staggers Act, especially with respect to captive rail shippers. NITL expresses its strong concern with the trend of cancellations of joint rates and through routes, as well as terminations of reciprocal switching arrangements.

NITL and AAR view the Staggers Act's objective of strong intramodal rail competition as crucial. Both assert that while the proffered rules are not a complete answer, they would contribute to solving the problems with competitive access, and they offer the proposed rules in the spirit of reducing government regulation and of promoting negotiated settlements.

The rules proposed by AAR and NITL consist of six parts.[7] Part (a) requires notice and explanation of any proposed joint rate cancellation, and establishes time limits for those actions. Part (b) requires negotiation between those proposing a cancellation and prospective opponents before any proceeding challenging the cancellation can be brought. Parts (c), (d), and (e) detail how the Commission would decide whether to suspend a proposed cancellation, under what circumstances the Commission would find a cancellation unlawful if it suspends and investigates, and the factors the Commission would consider in prescribing a through rate or route or reciprocal switching. Parts (d) and (e) specifically indicate that in exercising its prescription authority, the Commission shall not consider product competition, and that the railroad would have the burden of proof if it wishes to rely on geographic competition. In addition, both parts preclude denying relief solely on the basis of a railroad's revenue inadequacy. Part (f) states that determinations under Parts (d) and (e)(3) will have no collateral estoppel or res judicata effect in any Federal antitrust actions. This agreement is reproduced in Appendix A.[8]

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[4] Bessemer & Lake Erie Railroad Company; Elgin, Joliet and Eastern Railway Company; Florida East Coast Railway Company (which does not agree with the entire proposal); Grand Trunk System; Green Bay and Western Railroad Company; Milwaukee Railroad; MIssouri-Kansas-Texas Railroad Company; Pittsburgh & Lake Erie Railroad; and Soo Line Railroad Company.

[5] Before any agency issues substantive rules, the APA requires that it must publish a general notice of proposed rulemaking in the Federal Register, and must give "interested persons an opportunity to participate in the rulemaking through submission of written data, views, or arguments." 5 U.S.C. 553(b) and (c).

[6] The relevant exception to this requirement is when "the agency for good cause finds . . . that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest," 5 U.S.C. 553(b(B). However, the courts have emphasized that this exception is to be "narrowly construed and only reluctantly countenanced." American Federation of Government Emp. v. Block, 655 F. 2d 1153, 1156 (D.C. Cir. 1981) quoting State of N.J. v. U.S. Environmental Protection Agency, 626 F.2d 1038, 1045 (D.C. Cir. 1980) See also Buschmann v. Schweiker, 676 F.2d 352, 357 (9th Cir. 1982) (the "good cause exception is essentially an emergency procedure"; it must be interpreted "narrowly" so that "the exception will not swallow the rule").

[7] The Appendices reflect part "numbers" as they would appear if codified. Those part "numbers" are used here for convenience.

The RAM proposal is designed to address the concern of small regional railroads that cancellation by large carriers of their joint rates and through routes adversely affects their ability to compete. RAM participated in the Ex Parte No. 456 negotiations and asserts that early in that negotiating process its basic proposals were acceptable to all but AAR and Conrail. It sees its member railroads as the victims of joint rate cancellations and does not believe the AAR/NITL agreement offers its members effective relief.

The RAM proposal also has six parts. Part (a) provides standards for suspension of joint rate and through route cancellations, including a 10-day period during which the proponent carrier, if asked, must justify its proposal. Parts (b) and (c) establish the standards we would use in ruling on the lawfulness of such cancellations in suspension and complaint proceedings. Part (d) is a corollary to Parts (b) and (c) in that it establishes standards to be used for prescribing through routes and joint rates. The Commission would be prohibited from considering product and geographic competition and revenue adequacy or inadequacy in a through route or joint route prescription proceeding. Part (e) sets forth the grounds for prescription of reciprocal switching and the maximum charge therefor. This section is not applicable to certain categories of carriers. Part (f) governs prescription of terminal trackage rights, prescribes the status of the tenant vis-a-vis the owning carrier and contains the same exception for certain carriers as is in Part (e). This agreement is reproduced in Appendix B.

DISCUSSION AND CONCLUSIONS

In Ex Parte No. 445, supra, we reached a number of conclusions, some of which bear repeating here. First, we noted that many (but not necessarily all) of the rate, route, and switching cancellations were the type of changes Congress expected in enacting the Staggers Rail Act of 1980. Second, we were concerned that no rules had been proposed and that petitioners' generalized concerns expressed as rules would be ineffective to deal with particular cases. Nevertheless, we recognized that a problem existed and have sought ways to resolve it. Ex Parte No. 456 may have been helpful to the extent it provided a forum for private discussions that have narrowed the issues and established some common ground.

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[8] On March 12, 1985, AAR and the Chemical Manufacturers Association filed a joint petition for rulemaking on competitive access issues. They state that the terms of the AAR/CMA agreement are substantially similar to, and entirely consistent with, the standards previously proposed by AAR/NITL, but that the AAR/CMA agreement clarifies the AAR/NITL agreement. This petition will be treated as a comment, and must be served on parties to this proceeding when the service list is served. Also, because the petition has been served on all parties to Ex Parte Nos. 445 and 456, we will accept comments on the AAR/CMA agreement.

We are encouraged by the signing of the AAR/NITL agreement. It is a step forward from our Ex Parte No. 445 decision and reflects an appreciation of the concerns we expressed there. While even those parties agree that it does not satisfy all of the preferences of all members of both groups, it is clear evidence that traditional adversaries can reach a meeting of the minds on issues important to both. The RAM proposal, addressing as it does the concerns of certain regional carriers, will also be very important in focusing our inquiry and ensuring that the legitimate interests of these parties are protected.

We have now been offered two quite different proposals addressing the group of concerns termed competitive access. Our resolution of the problem through rules we will adopt in this proceeding must be responsive to two basic principles. First, the rules must be consistent with statutory requirements. Second, they should be acceptable to as broad a section of the marketplace as is possible. The more support that exists for the adopted rules, the more effective they will be in minimizing the need for regulatory intervention. 49 U.S.C. 10101a (the Rail Transportation Policy), and the Staggers Act in general, evince a Congressional interest in private dispute resolution and minimized Federal involvement.

The two proposals are useful to focus public comment because they are quite different in a number of respects. The NITL/AAR agreement addresses the problem in relative terms, for example, comparing pre- and post-cancellation revenues and costs. The RAM proposal sets certain absolute rate ceilings based on costs and uses costs tests as the basis for ICC intervention and prescription of remedies. While both contain 10-day "justification" provisions, the AAR/NITL agreement also requires prior attempts at private resolution of the disagreement. Overall, and at the risk of oversimplifying, the basic difference in approach is that the RAM proposal contains defined standards which do not need further development (see e.g., the Part (b)(1) and Part (c)(1) alternative tests of unlawfulness) while the AAR/NITL agreement addresses the problem in more general terms, requiring balancing of many competing factors and all relevant circumstances.

Given all of the foregoing, we are proposing to adopt the rules in Appendix A which are the product of negotiations between two broadly based industry groups, AAR and NITL. As an alternative, we are proposing the rules in Appendix B, offered for our consideration by RAM. In so doing, we do not intend to imply that we seek to polarize comments in an either/or way, or to imply that we will adopt in its entirety one or the other of these quite different proposals. To the contrary, our purpose is to comply with the legal requirements for adequate notice of the nature and breadth of the subjects and issues we intend to consider. We seek not only comments on these two proposals, but also suggestions for modifications or combinations, and their justifications. Having been informed by the public comments and suggestions, our final rules may be different from either of the proposals set forth in this Notice.9/ Cf., American Iron & Steel Inst. v. EPA, 568 F.2d 284, 293 (3rd Cir. 1977); Ethyl Corp. v. Environmental Protection Agency, 541 F.2d 1, 48-49

9/ Changes to 49 C.F.R. 1312 may also be required, should, for example, a change in the notice period be adopted.

(D.C. Cir. 1976); Air Transport Ass'n of America v. CAB, 732 F.2d 219, 2224-225 (D.C. Cir. 1984).

We believe most of both proposals are self-explanatory. However, there are a number of aspects on which we request further explanation. We pose these as questions:

Both Proposals

1. Is it the petitioners' intention that the stated circumstances would be the only ones under which the Commission would suspend competitive access disputes?

2. Do the caveats/prohibitions on use of geographic and product competition reflect an agreement among the parties that intermodal competition is relevant and should be considered in competitive access proceedings?

3. Are the 49 U.S.C. 10705a protections regarding Class III carriers intentionally outside the scope of the proposals?

4. How do the parties intend the Commission define "would utilize", in Parts (c) and (e) of the NITL/AAR agreement and Part (e) of the RAM proposal? Is a simple allegation intended to be sufficient?

5. Are the rules intended to have only prospective effect, or do the parties intend that they be applied to pending cases?

NITL/AAR Agreement

6. What role, if any is the Commission expected to play in implementing Part (f) of the agreement?

7. What is included in the term "costs" as used in Parts (d) and (e)?

8. The Union Pacific has expressed concern that the agreement does not preserve the distinction between the statutory standards for reviewing proposed cancellations [49 U.S.C. 10705(e)(1)] and those for establishing new joint rates and through routes [49 U.S.C. 10705(a)(2)]. Is this concern warranted?

RAM Proposal

9. What is the effect of Parts (e)(5) and (f)(1)?

10. What is intended by Part (f)(2)?

PROCEDURAL MATTERS

Anyone interested in participating in this proceeding must notify the Commission, in writing, by (15 days after publication). The Secretary of the Commission will issue a service list by (30 days after publication). All comments must be served on all parties on the service list so that replies can be expeditiously prepared and filed.

CONCLUDING STATUTORY FINDINGS AND AUTHORITIES

This action will not significantly affect the quality of the human environment or energy conservation.

The Commission certifies that rules it adopts in this proceeding will not have a significant adverse economic impact on a substantial number of small entities, because such rules will not result in a lessening of intrarailroad competition.

AUTHORITY: 49 U.S.C. 10321, 10703, 10705, 10707, 11103 and 5 U.S.C. 553.

It is ordered:

1. The petitions for rulemaking are granted, and a rulemaking is instituted.

2. An original and 15 copies of comments must be filed by May 17, 1985, with replies due June 3, 1985.

3. Interested parties must notify the Commission, in writing, of their intent to participate by April 17, 1985. A service list will be issued by May 2, 1985 and all comments must be served on parties on the service list.

4. The previously filed NITL and PPG petitions, seeking a reopening or reconsideration of our decision in Ex Parte No. 445, are denied.

5. This decision is effective on the date served.

By the Commission, Chairman Taylor, Vice Chairman Gradison, Commissioners Sterrett, Andre, Simmons, Lamboley, and Strenio. Commissioner Strenio concurred with a separate expression.

James H. Bayne
Secretary

(SEAL)

Commissioner Strenio, concurring:

I wholeheartedly support this rulemaking proceeding, and I applaud the efforts of the parties to work together to achieve a reasonable compromise. I think we also could benefit, however, by re-shaping our questions to make it clear that we solicit comments and responses from all interested parties, not just from the petitioners.

In addition, we could benefit from comments on the effect on the proposals here of our treatment of product and geographic competition in a related rulemaking, Ex Parte No. 320 (Sub-No. 3).

APPENDIX A

Alternative 1, AAR/NITL Proposed Rules:

We propose to amend Chapter X of Title 49 of the Code of Federal Regulations by adding the following:

§1132.3 Through route and through rate cancellation regulations.

(a) Notification, explanation, and justification. A carrier proposing to cancel a through route and/or a joint rate shall publish notice of its intent to make such a cancellation forty-five days prior to the effective date of such cancellation. Upon request of any affected party seeking (a) an explanation of how the proposed cancellation would affect such party, or (b) justification for the cancellation as it would apply to a route or rate actively utilized or participated in by such party, the carrier proposing to cancel shall provide such explanation or justification within ten days.

(b) Negotiation. Prior to bringing any proceeding challenging a cancellation or seeking the prescription of a through route or through rate, any party intending to initiate such a proceeding shall first seek to enter into negotiations to resolve its dispute with the prospective defendants in any such proceeding. Any such party may bring a proceeding challenging a cancellation or seeking prescription of a through route or through rate five days after seeking to enter into negotiations, if such negotiations have not successfully resolved the dispute. Participation in such negotiations does not waive a party's right to file a timely petition for suspension for investigation.

(c) Suspension for investigation of a proposed through route and/or joint rate cancellation. The ICC shall suspend for investigation a proposed cancellation of a through route and/or a joint rate if it determines:

(1) that a protesting shipper has utilized the through route and/or joint rate proposed to be cancelled to meet a significant portion of its current or future railroad transportation needs; or

(2) that a protesting carrier has utilized or would utilize the affected through route and/or joint rate for a significant amount of traffic; and

(3) that such cancellation would eliminate effective railroad competition for the affected traffic between the origin and destination.

(d) Investigation of cancellations. In investigating a proposed cancellation of a through route and/or a joint rate, the Commission shall determine that the cancellation is contrary to the public interest under 49 USC 10705 if it finds that the cancellation, or a rate that would remain in place after the cancellation, is contrary to the competition policies of 49 USC 10101 or is otherwise anticompetitive. In making its determination, the Commission shall take into account all relevant factors, including:

(1) factors relevant under 49 USC 10101a and 10705, including 10705(e)(1);

(2) the revenues of the involved railroads on the affected traffic via the rail routes in question;

(3) the efficiency of the rail routes in question, including the costs of operating via those routes;

(4) the rates charged or sought to be charged by the cancelling railroad or railroads;

(5) the revenues, following the cancellation, of the involved railroads for the traffic in question via the affected through route; the costs of the involved railroads for that traffic via that route; the ratios of those revenues to those costs; and all circumstances relevant to any difference in those ratios provided that the mere loss of revenue to an affected carrier shall not be a basis for finding that a cancellation is anticompetitive.

However the Commission shall not consider product competition; and if a railroad wishes to rely in any way on geographic competition, it shall have the burden of proving the existence of such competition by clear and convincing evidence. Any investigations of cancellations under the terms of this paragraph will be conducted and concluded by the Commission on an expedited basis. Where a cancellation has been determined to be contrary to the competitive standards of this section, the overall revenue inadequacy of the cancelling carrier shall not excuse such a cancellation.

(e) Establishment of through routes, through rates and reciprocal switching. A through route or a through rate shall be prescribed under 49 USC 10705 or reciprocal switching shall be established under 49 USC 11103 if the Commission determines:

(1) that the complaining shipper has utilized or would utilize the through route, through rate or reciprocal switching to meet a significant portion of its transportation needs; or

(2) that the complaining carrier has utilized or would utilize the through route, through rate or reciprocal switching for a significant amount of traffic; and

(3) that the prescription or establishment is necessary to remedy or prevent an act contrary to the competition policies of 49 USC 10101a or which is otherwise anticompetitive. In making its determination, the Commission shall take into account all relevant factors, including:

(i) factors relevant under 49 USC 10101a and 10705, including 10705(e)(1);

(ii) the revenues of the involved railroads on the affected traffic via the rail routes in question:

(iii) the efficiency of the rail routes in question, including the costs of operating via those routes;

(iv) the rates charged or sought to be charged by the cancelling railroad or railroads;

(v) the revenues, following the prescription, of the involved railroads for the traffic in question via the affected route; the costs of the involved railroads for that traffic via that route; the ratios of those revenues to those costs; and all circumstances relevant to any difference in those ratios; provided that the mere loss of revenue to an affected carrier shall not be a basis for finding that a prescription or establishment is necessary to remedy or prevent an act contrary to the competitive standards of this section.

However, the Commission shall not consider the product competition; and if a railroad wishes to rely in any way on geographic competition, it shall have the burden of proving the existence of such competition by clear and convincing evidence. When a sought prescription of a through route, through rate or reciprocal switching is necessary to remedy or prevent an act contrary to the competitive standards of this section,the overall revenue inadequacy of the defendant railroad(s) shall not be a basis for denying the sought prescription.

(f) Effect of Commission determinations or findings under the standards set forth here. Any Commission determinations or findings under the preceding paragraphs with respect to compliance or non-compliance with the standards of paragraph (d) or paragraph (e)(3) of this section shall not be given any res judicata or collateral estoppel effect in any litigation involving the same facts or controversy arising under the antitrust laws of the United States.

APPENDIX B

Altenative 2, RAM Proposed Rules:

We propose to amend Chapter X of Title 49 of the Code of Federal Regulations by adding the following:

§1132.3 Through route and through rate cancellation regulations.

(a) Notification, justification and standards for suspension. The ICC shall suspend for investigation a proposed cancellation of a joint rate and/or through route if it determines:

(1) that such cancellation would reduce effective railroad competition for the affected traffic between the origin and destination, or any portion of the affected routes; or

(2) that the mileage between origin and destination over the joint rate or route proposed to be cancelled or closed is not more than the mileage between the same origin and destination over the joint rates and through routes that would remain in effect after the cancellation; or

(3) that the ratio of revenue to variable cost for the cancelling railroad under the affected joint rate and through route is equal to or greater than the lowest ratio over the cancelling railroad's alternative joint or single line routes on the affected traffic between the origin and destination involved; or

(4) that within ten days after receipt of a request for such explanation and justification that the cancelling railroad failed to provide a full explanation and justification for the cancellation as it would apply to a rate or route utilized or participated in by the requesting party, including relevant mileage, revenue and variable cost data adequate to compare efficiency and profitability.

(b) Investigation of cancellations. In an investigation of a cancellation of a through route and/or joint rate, the Commission shall determine that the cancellation is not consistent with the public interest under 49 U.S.C. 10705 if it finds that:

(1) the ratio of revenue to variable cost for the cancelling railroad under the affected joint rate and through route is equal to or greater that the lowest ratio over the cancelling railroad's remaining alternative single or joint line routes on the affected traffic between the origin and destination involved; or

(2) that such cancellation would reduce effective railroad competition for the affected traffic between the origin and destination, or any portion of the affected routes.

(c) Complaint proceeding regarding cancellations. In a complaint proceeding regarding a cancellation of a through route and/or joint rate, the Commission shall determine that the cancellation is not consistent with the public interest under 49 U.S.C. 10705 if it finds:

(1) that the ratio of revenue to variable cost for the cancelling railroad under the affected joint rate and through route is equal to or greater than the lowest ratio over the cancelling railroad's remaining alternative single or joint line routes on the affected traffic between the origin and destination affected; or

(2) that such cancellation would reduce effective railroad competition for the affected traffic between the origin and destination, or any portion of the affected routes.

In a complaint proceeding, the cancellation of a through route or joint rate shall be presumed to violate the public interest standard of section 10705 if the complainant demonstrates that the route at issue is of reasonably comparable or superior efficiency to any competitive rail route in which the cancelling carrier participates, and the rates of the cancelling carrier will reduce effective railroad competition for the traffic at issue. The cancelling carrier may rebut the presumption by a showing that the cancellation or subsequently applicable rates will not reduce effective railroad competition for the traffic at issue.

(d) Establishment of through routes and joint rates.

(1) Upon petition of an interested party or on motion of the Commission, a through route or joint rate shall be prescribed if the Commission determines:

(i) that the prescription or establishment is necessary to remedy or prevent an act or condition that is contrary to the competition policies of 49 U,S.C. 10101a, or that is otherwise anticompetitive; or

(ii) that the ratio of revenue to variable cost for any nonconcurring railroad is no lower than the lowest ratio over the alternate joint or single line rail routes on the affected traffic between the origin and destination affected.

(2) In making its determination, the Commission shall take into account all relevant factors, including:

(i) whether the prescription or establishment is necessary to provide effective railroad competition for the affected traffic between the origin and destination, or any portion of the affected rates, and

(ii) the efficiency of the rail routes in question, and

(iii) the comparison of the revenues and variable costs of all involved railroads over the alternative routes,

except that product and geographic competition and revenue adequacy and inadequacy shall not be considered.

(e) Prescription of reciprocal switching and charges. Reciprocal switching shall be prescribed by the Commission upon an application filed by a shipper or carrier who demonstrates said switching is either practicable and in the public interest or necessary to provide competitive rail service if the Commission determines:

(1) That a shipper has utilized or would utilize such reciprocal switching to meet a significant portion of its current or future transportation needs; or

(2) that the complaining carrier has utilized or would utilize such reciprocal switching for a significant amount of traffic.

(3) Charges for reciprocal switching established by the Commission shall not exceed the fully allocated cost of providing such service.

(4) Any establishment or prescription under the terms of this paragraph will be conducted and concluded by the Commission on an expedited basis.

(5) The provisions of this paragraph are inapplicable if the carrier physically serving the industry is a Class III, Class II or Class I railroad having less than two percent of the railroad industry gross freight revenue.

(f) Prescription of terminal trackage rights. Terminal trackage rights, including main line tracks for a reasonable distance outside of a terminal shall be prescribed by the Commission upon an application filed by a carrier who demonstrates said trackage rights are practicable and in the public interest, unless the owning carrier establishes that the granting of an application would substantially impair its ability to handle its own business:

(1) The foregoing provision is inapplicable if the owning carrier is a Class III, Class II or Class I railroad having less than two percent of railroad industry gross freight revenues.

(2) To accomplish the objectives of 49 U.S.C. 1103(a), charges for terminal trackage rights established by the Commission shall put the tenant in the same position as the owning carrier.

(3) Any establishment or prescription under the terms of this paragraph will be conducted and concluded by the Commission on an expedited basis.

The Chairman. And also I am going to allow his counsel, if you will come up to the table here, to propound questions today that Senator DeConcini had prepared.

Our first witness today is Mr. Charles F. Rule, Acting Assistant Attorney General, Antitrust Division.

Mr. Rule, you may proceed.

STATEMENT OF HON. CHARLES F. RULE, ACTING ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, U.S. DEPARTMENT OF JUSTICE

Mr. Rule. Thank you, Mr. Chairman.

I understand that my statement has been distributed to the members. I would appreciate it if it could be entered into the record and, for the sake of time, I will try to summarize my remarks here today.

The Chairman. All right.

Without objection, your entire statement will go into the record, and if you will just summarize it.

Mr. Rule. Thank you, sir.

The Chairman. Now, when we say summarize, we do not mean actually read the statement.

Mr. Rule. Yes, sir.

The Chairman. We put your whole statement in the record so you just give us a thrust.

Mr. Rule. Yes, sir.

I am pleased to be here to present the views of the Department of Justice on S. 447, the Railroad Antimonopoly Act of 1985. As you know, the act would add a new section to the Sherman Act, making it unlawful for a railroad that provides sole rail access to a shipper or receiver of bulk commodities to monopolize, or to attempt to monopolize, by denying use on reasonable terms of its sole facilities to competing carriers.

If the railroad does not permit use of its facilities, or if no rail competition materializes, the bill would require the rail carrier to charge rates no higher than would yield a fair return on the proportion of the owner rail carrier's prudent investment in the sole rail facility.

In addition to these and other substantive provisions, the bill would provide for injunctive relief and treble damage relief for breach of its provisions.

The scope and severity of the so-called captive shipper problem we believe has not yet been established. As a result, and because of certain specific objections to provisions in the bill, the Department opposes the enactment of S. 447.

First of all, as I said, the captive shipper problem has not yet been, I do not think, at least the evidentiary record has not yet been, fully developed. There is, to be sure, anecdotal evidence of problems in this area, but we think more needs to be developed.

We also think it is unclear, even though we have heard some of these criticisms, that the Staggers Act is not adequate and that the ICC's enforcement is deficient in this area. But again we think that more study of that needs to be done.

Moreover, we believe that in addressing problems in this area, it is important that this problem not be used as an excuse, as the backdoor, to reregulation or otherwise be allowed to undercut the goal of the Staggers Act.

Specifically as to S. 447, our objections fall into roughly three categories. First, the bill appears to be overbroad in that it provides severe regulatory remedies where there may be no competitive problems. The bill appears to ignore certain forms of competition that may constrain the ability of sole rail facility carriers to exploit any power over price. For example, the bill does not appear to take into account such things as source competition, that is competition may exist that constrains rates when wheat, for example, from Nebraska competes in Chicago with wheat from Oklahoma. The ability of a sole rail facility in Nebraska to raise its prices to the wheat farmers there may be constrained by the fact that if it does so, wheat in Oklahoma will be more prevalent in the market in Chicago because the rail carriers there compete and keep rates down.

Second, the bill appears to ignore intermodal competition, that is, competition to the sole rail carrier from trucks or barges. Particulary this is troublesome in the case of trailer on flatcar movement, that is TOFC movements, because in that area, in particular, truck competition can be significant.

Thus, we believe the bill to a large extent provides relief where there is no competitive problem. Its overbreadth is particularly troublesome given the rather substantial costs that the bill may impose. First, as in the case of almost all regulatory legislation, and we think this falls in that category, there are the normal administrative costs of enforcement and compliance on the part of the parties who have to comply.

In addition, it may create market distortions as a result of forcing rates to be charged that are below those that would be charged in a competitive market. This is particularly true where there are no competitive problems and competition exists. If the rates are found unreasonable and lower rates are forced to be charged, then there may not be an adequate return, or at least the return that the market would provide to a railroad on its investment. This can create a number of distortions, overutilization of track, the failure of railroads to make socially efficient investments and that sort of thing that we are very concerned about.

Second, even if S. 447 were limited to instances where there are competitive problems, we believe that it is largely redundant, that there are already effective remedies available to shippers. Captive shippers, as many of you may know, have structural remedies under the Interstate Commerce Act for reciprocal switching. Generally it is limited to situations where track is switching, not long-haul tracks. This reduces the threat of distortions.

In addition, the showing required for relief is minimal. We have heard that the ICC is not adequately enforcing this provision, as I mentioned earlier. However, we do not monitor in each case the factual records and we cannot really indicate whether or not that criticism is justified. However, I think the fact that the Commission is currently in the midst of a rulemaking proceeding in this area indicates that it is aware of the perceived problem and is looking into it, and it may come up with a solution on its own if there is indeed a problem.

I think at the very least we should wait for the outcome of that proceeding before taking any further action.

Third, we are troubled that the bill converts the Sherman Act from a statute that checks anticompetitive abuses, as it has historically, to one that regulates market forces. Regulation where necessary is essentially an executive branch function, not a judicial one. The courts are ill-equipped to regulate prices. The fact that there are numerous courts and numerous circuits may lead to disparate results around the country and nonuniform application of the policy even with regard to a single railroad. This problem is exacerbated by the fact that the act would provide a treble damage remedy, which is particularly inappropriate given the fact that various terms of the bill are very vague and subjective.

In conclusion, S. 447 indiscriminately provides potentially complex and intrusive regulatory solutions without requiring a showing of actual competitive harm.

Conversely, existing law already provides adequate remedies in reciprocal switching situations where intramodal competition can be increased with minimal regulatory intervention, and in situations where denial of access to an essential rail line constitutes monopolization of a relevant market. Enforcement of the bill thus would be overbroad and wasteful in some areas and unnecessary in others.

Having stated the Department's opposition to S. 447, I want to assure the committee that we hope that these hearings will develop evidence that will permit an objective evaluation of the scope and severity of the perceived captive shipper problem. Until an adequate evidentiary record is available, any legislation on this subject is not likely to have the beneficial effects that its sponsors certainly seek.

That concludes my remarks, and I would be happy to answer any questions the committee might have.

[Prepared statement follows:]

PREPARED STATEMENT OF CHARLES F. RULE, ACTING ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION

Mr. Chairman and members of the committee, I am pleased to be here today to present the views of the Department of Justice on S. 447, the "Railroad Antimonopoly Act of 1985." S. 447 is similar in concept to S. 2417 introduced during the previous Congress and is designed to provide relief to so-called "captive rail shippers."

S. 447 would amend the Sherman Act by adding a new section that would apply to any rail carrier that controls facilities providing the sole rail access to shippers or receivers of bulk commodities. The new section would make it unlawful for such a railroad to monopolize or attempt to monopolize trade by denying use of its sole facilities to competing carriers on reasonable terms. No violation of this provision would occur if such rail carrier permits another railroad offering competing service to use, on "reasonable terms," its facilities that provide access to the captive shipper. If the rail carrier does not permit such use of its facilities, or if no competition materializes from any competing rail carrier, the bill would prohibit a railroad owner of a sole facility from charging commodity rates in excess of a standard defined in the bill. The bill would also make it unlawful for the owner rail carrier to (1) condition the use of sole railroad facilities on the use of other facilities; and (2) suspend or threaten to suspend service over the sole facility by reason of a shipper's asserting its rights under this section. The bill would permit persons injured by violation of its substantive provisions to sue for treble damages as well as injunctive relief under the antitrust laws.

The "captive shipper" issue is one to which both the Department of Justice in particular and the Administration as a whole are giving close attention. For several reasons, however, we oppose S. 447. First, it is not clear that there is any significant captive shipper problem that cannot be remedied by existing statutes and administrative procedures. While we have heard anecdotal evidence about instances in which shippers have felt themselves unfairly treated by railroad carriers, it is not clear that the protections provided to captive shippers under the Staggers Act are somehow deficient or that the Interstate Commerce Commission is failing to implement the mandate it received from Congress in that Act less than five years ago. Indeed, the Commission is currently engaged in a proceeding to determine how well the Staggers Act has worked in protecting the interests of shippers.

Moreover, this bill fails to consider whether railroads earn adequate revenues, one of the primary goals of the Staggers Act. To the extent that the regulatory provisions of the bill would prevent railroads from earning competitive rates of return with the result that rail lines deteriorate and railroads go bankrupt, both railroads and shippers will be losers.

Second, even if there were hard evidence of a problem that should be addressed by new legislation, S. 447 is a very unsatisfactory answer because it would impose a drastic new regulatory regime upon an industry that has only recently begun to enjoy the benefits or deregulation. In my testimony today, I would like to describe our specific concerns with S. 447. Our objections to the bill fall into three categories: (1) the overbreadth of the bill in that it provides a remedy in many cases where there is no competitive problem; (2) the fact that the case has not been made that current remedies are inadequate; and (3) the problems of trying to transform the antitrust laws into a judicially imposed scheme of industry-specific regulation.

(1) We believe that S. 447 is overly broad in its assumption of what constitutes a competitive problem. Section 3 of the bill would add a new section to the Sherman Act that would make it unlawful "to monopolize or attempt to monopolize by denying or threatening to deny to any shipper or another rail carrier the use on reasonable terms of a railroad facility which is the sole facility over which such shipper can move bulk commodities by rail. . . ." Thus, the bill would appear to impose antitrust liability on a "sole facility" railroad regardless of the existence of other factors that constrain the railroad's ability to charge monopoly rates.[1]

Although the bill does not use or define the term "captive shipper," the bill's sanctions would apply whenever a railroad owns "the only facility by which a shipper can move bulk commodities by rail" to a competing railroad or to their destination.[2] Thus, the bill assumes the existence of a competitive problem whenever a single rail line is available to a shipper. This assumption, however, ignores the fact that even for shippers that have no practial access to other railroads, rail rates are often constrained by other factors, such as source competition from other railroads or intermodal competition. For example, if other shippers of the same commodity to the same market are served by different railroads, the rates the railroad can charge the "captive" shipper are constrained by the rates available to other sellers of the same commodity. This is so because if the transportation rate for one of those movements increases the final price of that commodity as compared with the price of the same commodity available from another location, purchasers can be expected to choose the lower-priced commodity. And the railroad seeking to exploit its captive shippers will lose traffic to other railroads transporting competing products at lower rates. Thus, the final product cost will constrain the ability of a railroad or other carrier to charge supracompetitive rates even though, in the terms of the bill, it is a "sole facility" rail carrier.

Similarly, large shippers of bulk commodities, such as grain, may have a number of different facilities from or to which they ship their commodities. Each of those facilities may be captive to a sole facility railroad. However, so long as the shipper's facilities collectively are served by a number of railroads, the shipper may be able to play the railroads off against one another. For example, if one railroad tries to exploit a facility it holds captive, the shipper can threaten to decrease its shipments from or to that facility and increase shipments from or to its other facilities served by other railroads charging lower rates.

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[1] If the bill, instead, is merely an attempt to incorporate the current standard of section 2 of the Sherman Act, 15 U.S.C. § 2, and thus would require a showing that the railroad actually possessed or had a dangerous probability of achieving, monopoly power, we would still oppose the bill. First, if it does not purport to change current law, it is unnecessary and would create uncertainty as to how the courts would interpret it. Second, because of the bill's numerous other standards that would require judicial regulation as described below, it would impose intolerable burdens on the courts.

[2] § 9; § 9(e)(4).

Moreover, for many commodities—including bulk commodities such as grain—railroads can and do face competition from trucks or barges. For example, close proximity to waterways may make barge or truck/barge movements of bulk commodities competitive with rail movements. Even if the railroad does not face intermodal competition for long-haul shipments, short-haul movements to other competing railroads may face intermodal (e.g., truck) competition. The bill, however, presumes that connections to competing railroads must be made via rail. In addition, S. 447 includes trailer-on-flatcar (TOFC) movements in its definition of bulk commodities, even though TOFC traffic is generally subject to intermodal competition, and subject to intramodal competition where origins or destinations are within trucking distances of alternative railroads.

Because of its well-known pitfalls, regulatory-type relief should only be available, in the courts or elsewhere, in the most compelling circumstances, where its benefits clearly outweigh its costs. As indicated above, this bill would impose antitrust liability and make regulatory-type relief available without the necessity of establishing that a competitive problem exists. A plaintiff need not show that there is a relevant market where the rail carrier has the power to control prices or exclude competition ("monopoly power"), as a plaintiff currently must show under Section 2 of the Sherman Act.[3] A plaintiff need show only that a shipper is not served directly by a second railroad—a common situation—and that the sole facility railroad has refused to make access available on the statutory terms, or that, having made such access available, no rail competiton has materialized for that traffic. Such a showing falls far short of proving that monopoly power is actually present and does not establish the presence of any competitive problem that requires regulatory-type intervention.

S. 447 seems to contemplate a remedy similar to that provided by the "essential facility doctrine" that has developed in the case law under Section 2 of the Sherman Act. Under that doctrine, fair access to an essential facility must be provided to competitors when access is necessary in order to compete in a relevant market, the facility cannot reasonably be duplicated by competitors, and access can be granted without interfering with the owner's use of the facility.[4] Even the "essential facility" doctrine, which requires a showing of monopoly power, has proven difficult to apply in practice and can be criticized as denying the facility's owner a legitimate return on its investment. Loosening the standards of the doctrine to the extent contemplated by S. 477 and thereby expanding the scope of the power of the courts to replace market forces with judicial fiat could well lead to seriously adverse results in the marketplace.

Imposing regulatory-type rules on railroads that lack market power is unnecessary, wasteful, and completely inconsistent with the purposes of rail deregulation. As articulated by Congress in the Staggers Act, the national rail policy seeks to minimize the need for regulatory control over the rail industry.[5] Where competitive forces make regulation unnecessary, its use is wasteful not only because of the substantial administrative costs to the government and the parties of litigating and enforcing the regulation, but also because the rule itself may lead to inefficient results. If a carrier currently providing rail service at competitive rates is required to grant access over its lines, market distortions will occur unless the trackage right rental rate covers the true cost of providing access to the second carrier. If the rental is set too low, investment in the facility will decrease, and service to the shipper will deteriorate. If a court happens to find the terms set by competitive forces to be unreasonable, then the carrier faces not only the prospect of a court-decreed reduction in the rate but also an automatic treble damage penalty for the overcharge. Thus, when regulation is attempted with respect to significant segments of a carrier's trackage, the chances of setting the proper rate are reduced and the adverse impact of the error is increased.

Because shippers can be expected to use the proposed remedies to obtain lower shipping rates, even when the rates are already competitive, the bill also seriously threatens to undercut the goal embodied in the Staggers Act of enabling railroads to earn a competitive rate of return. The history of rate of return regulation generally has been to undercompensate regulated entities for their investments. In particular, the risk of investments tends to be underestimated with the result that the regulated firms earn less than a market rate of return. The effect is to discourage socially beneficial investment. This danger is manifest in S. 447's requirement that rates be "no higher than would yield a fair return on the proportion of the owner rail carrier's prudent investment in the sole railroad facility that the shipper's traffic bears to all traffic using such sole railroad facility." The fact that this directive will be enforced by courts that institutionally are not well suited to make such determinations and that may reach disparate results magnifies the potential threat to the railroads' ability to earn a market rate of return.

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[3] See *United States* v. *Grinnell Corp.*, 384 U.S. 563, 571 (1966).

[4] See *Otter Tail Power Co.* v. *United States*, 410 U.S. 366 (1973); *MCI Communications Corp.* v. *AT&T*, 708 F.2d 1081 (7th Cir. 1983), *cert. denied*, U.S. , 104 S. Ct. 234 (1983).

[5] 49 U.S.C. § 10101a.

(2) Even if the scope of S. 447 were limited to those situations where a competitive problem might arise, we would oppose the bill because it would not significantly add to the relief that is a available to captive shippers under existing law. Apart from maximum rate regulation under the market dominance provisions of the Interstate Commerce Act, captive shippers have structural remedies available under the Interstate Commerce Act. Regulatory intervention to grant access is most justified where the enhancement of competition is great and the adverse effect on the efficient operations of the track-owning rail carriers is de minimis. This will most likely be the case where access is granted over short distances on limited-use track. If the "sole facility" is such that the shipper is accessible through switching services, the shipper or a competing carrier can petition the ICC to order reciprocal switching under 49 U.S.C. § 11103(c), a provision added by the Staggers Act. The Commission is authorized to set the rail carrier's compensation, if necessary. All that is required for the shipper to obtain relief under § 11103(c) is a showing that there is no alternative intramodal competition.[6] However, unlike S. 447, which potentially authorizes a grant of trackage rights over mainline or important branch lines, a § 11103(c) proceeding does not threaten to create significant inefficiencies, for regulated access is limited to segments of track that can reasonably be characterized as switching and hence are less crucial to a carrier's overall operations.

We are aware of the criticism that has been leveled at the ICC for failing to grant relief as often as complainants would like under the market dominance and reciprocal switching provisions of the Staggers Act. The Department does not normally monitor the factual records in such cases, and we cannot say the criticsm is justified. However, the ICC has recently published a notice of its intention to adopt rules for handling captive shipper situations.[7] The Commission is seeking comments on a joint proposal of the Association of American Railroads and the National Industrial Traffic League. If adopted as published, this rule would increase the ease with which captive shippers could obtain relief. In cases involving reciprocal switching or joint rate cancellations, the rule would preclude consideration of product competition, require the railroad to demonstrate source competition by clear and convincing evidence, and make irrelevant the issue of the adequacy of the railroad's revenues.

The Department is currently studying the proposal. Regardless of our eventual conclusion, however, we believe that the current rulemaking proceeding shows that the ICC is aware that problems may exist and is considering what steps, if any, should be taken consistent with the Staggers Act. At the very least, it would be premature for the Congress to act before first observing the outcome of the ICC's current proceeding.

(3) In addition to the other problems associated with S. 447, we are much troubled, as a general matter, by any effort to transform the antitrust laws into a special purpose regulatory statute administered by the courts. The antitrust laws are not designed to supplant the market mechanism which, as those laws recognize, is generally best able to bring into balance the forces of supply and demand. Instead, the antitrust laws are designed to protect competition so that market forces themselves can regulate supply and demand. As such, the antitrust laws generally require case-by-case adjudication, rather than industry-wide, sector-wide, or economy-wide regulation. However, if there is a need to regulate conduct (and we reiterate that no showing has yet been made that would necessitate regulation beyond that provided for in the Staggers Act), that responsibility should not be delegated to the courts.

Regulation where necessary is essentially an Executive Branch function, not a judicial one. The proper resolution of the issue of what constitutes a proper rate frequently is beyond the institutional competence of a court. Moreover, because of the number of different courts of appeals that might issue conflicting judgments, it is highly unlikely that the regulatory scheme will be imposed uniformly, increasing uncertainty and the possibility that a single railroad with a presence in a number of different circuits would—at least in the short term—be subject to different interpretations of the bill's regulatory requirements.

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[6] Under § 11103(c), the Commission may order switching if it is "practicable and in the public interest," or where "necessary to provide competitive rail service."

[7] Ex Parte 445 (Sub. No. 1), *Intramodal Rail Competition*, 50 Fed. Reg. 13051 (April 2, 1985).

These problems are substantially exacerbated by the fact that, under the bill, a captive shipper can obtain not only injunctive relief but also treble damages. Given the number of questions that have been raised about the wisdom of the general applicability of automatic treble damages, we seriously question whether it is wise further to extend their application as proposed in S. 447. This is particularly true because, given the vagueness and subjective nature of the bill's reference to "reasonable terms" and "fair return," the treble damages remedy well might force railroads to charge rates other than those what would be obtained by competitive market forces in the absence of government interference. The result would be the inability of railroads to earn adequate revenue and the misallocation of resources.

In conclusion, S. 447 indiscriminately provides for potentially complex and intrusive regulatory solutions without requiring a showing of actual competitive harm. Conversely, existing law already provides remedies in reciprocal switching situations where intramodal competition can be increased with minimal regulatory intervention, and in situations where denial of access to an essential rail line constitutes monopolization of a relevant market. Enforcement of the bill thus would be overboard and wasteful in some areas and unnecessary in others. The Department of Justice recommends against enactment of this legislation.

Having stated the Department's opposition to S. 447, I want to assure the Committee that we hope that these hearings will help to develop evidence that will permit an objective evaluation of the scope and severity of the perceived captive shipper problem. Until an adequate evidentiary record is available, any legislation on this subject is not likely to have the beneficial effects that its sponsors certainly seek.

That concludes my prepared remarks, and I would be pleased to answer any questions the Committee might have.

The CHAIRMAN. Thank you very much.

I have a conflict, and I am going to ask Senator McConnell to take the Chair now. He has agreed to do so.

So, Senator McConnell, if you will come around and you can ask the questions.

We have placed more or less a limit of 5 minutes, but I think we might allow 7 or 8 minutes to the witnesses if they desire that much.

Senator MCCONNELL [presiding]. Thank you, Mr. Chairman.

I would like to ask unanimous consent that an opening statement of mine appear in the record. Without objection, that will be done.

[Statement follows:]

OPENING STATEMENT OF SENATOR MITCH MCCONNELL

Mr. Chairman, it seems that this hearing is particularly timely in light of the Committee's current inquiry into the antitrust implications of the Treasury's proposed sale of Conrail to the Norfolk and Southern Railroad. Many of the concepts, if not the issues themselves, that we will presumably discuss today are similar to those involved with the Conrail sale.

Yet the hearing is also timely because of the evolving nature of the field of antitrust. It is probably fair to say that over the past 10 to 15 years the area of antitrust law has not be the most conceptually consistent field that either the courts of the Congress has stepped into. Indeed, antitrust law has always been perhaps a bit arcane, and the problem has not been lessened in recent years with the far-reaching deregulation undertaken by the government in a number of fields.

The railroad industry is one of those fields, as we are all aware. The trend toward consolidation in the railroad industry, while not precisely the topic of today's hearing, should perhaps give us pause to consider the position we expect our rail industry to be in in 10 or 20 years. I believe this hearing is part of the process of reevaluation of the competitive status of the railroad industry that is essential to see that we don't inadvertently find ourselves one day with an industry devoid of meaningful competition or one tethered by unnecessary and counter-productive regulations and substantive rules of law.

I am looking forward to hearing the Justice Department's views on the extent to which there is a competitive problem with regard to captive shippers, especially since a written statement of the Department's views was not available before the hearing, as well as to hearing the testimony of the other witnesses today. Thank you, Mr. Chairman.

Senator McCONNELL. Senator Denton has joined us.

Senator Denton, do you have an opening statement or any questions you would like to ask the witness?

Senator DENTON. No; I will submit a statement for the record.

Senator McCONNELL. OK. And the Chairman has indicated that Mr. Feidler, Senator DeConcini's chief counsel, be permitted to ask questions since Senator DeConcini has broken his ankle and is unable to be here.

Mr. Feidler, since this is Senator DeConcini's bill, why do we not go to you and let you propound questions to the witness.

Mr. FIEDLER. Thank you, Mr. Chairman.

We will not have any oral questions of Mr. Rule. Senator DeConcini would like to submit some to him later if that is possible.

Senator McCONNELL. All right. That will be done, yes.

[Information follows:].

U.S. Department of Justice

Office of Legislative and Intergovernmental Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

[illegible] 7 1985

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Enclosed please find answers to the questions submitted by Senator DeConcini following the Committee's hearing on S. 447, the "Railroad Antimonopoly Act of 1985." I appreciate the opportunity to provide these answers for the record.

Sincerely,

Phillip D. Brady
Acting Assistant Attorney General

Enclosures

ANSWERS TO QUESTIONS FROM SENATOR DECONCINI REGARDING S.447, THE RAILROAD ANTIMONOPOLY ACT OF 1985

1. **What remedies for "captive shippers" do you refer to at p. 2 of your testimony?**

   A. The key remedies provided to captive shippers by the Interstate Commerce Act are the imposition by the Interstate Commerce Commission ("ICC") of maximum rate regulation under the market dominance provisions of 49 U.S.C. 10709, and of competitive access under the reciprocal switching or terminal facility provisions of 49 U.S.C. 11103. An indirect method of achieving similar results under some circumstances is through the ICC's authority to prescribe through routes, joint rates and the divison of joint rates, pursuant to 49 U.S.C. 10705(a). See also our answer to Question 2 below.

2. Do the remedies you refer to include antitrust remedies?

A. Yes. In order to obtain relief under the antitrust laws, an alleged captive shipper must demonstrate that a market for antitrust purposes can properly be defined to include the captive shipper's shipments and that such a market has been, or is likely to be, unlawfully monopolized by the rail carrier. If a captive shipper can demonstrate unlawful monopolization of that market by a rail carrier, the antitrust laws would provide both treble damage remedies (where not precluded by Keogh v. Chicago & Northwestern Ry., 260 U.S. 156 (1922), see infra, answers to questions 6-8) and equitable remedies (where not precluded by section 16 of the Clayton Act, 15 U.S.C. 26, see infra, answer to question 28).

Whether Keogh precludes treble damages in a particular monopolization suit brought by a captive shipper depends on the plaintiff's legal theory. Unless the plaintiff claims that the level of the defendant's tariff rates or charges were established in violation of the antitrust laws, and seeks damages measured by reference to that claimed illegal tariff level, Keogh would not preclude treble damage recovery. Section 16 appears to preclude injunctive antitrust relief compelling access where a shipper is eligible for reciprocal switching relief from the Commission under 49 U.S.C. 11103(c), but not in situations that involve access to a line haul monopoly rail link, an area in which the Commission has no regulatory jurisdiction.

3. What antitrust remedies are available to a captive shipper who is forced to pay unreasonable rates to a carrier with monopoly power over him?

A. A monopolist does not violate the antitrust laws simply because it exercises lawfully-obtained monopoly power by charging monopoly prices. In order to prevail on a claim of unlawful monopolization in violation of section 2 of the Sherman Act, 15 U.S.C. 2, a plaintiff must prove both (1) that the defendant possesses monopoly power in the relevant market; and (2) that the defendant has willfully acquired or maintained that power, as distinguished from achieving it through "a superior product, business acumen, or historic accident." United States v. Grinnell Corp., 384 U.S. 563, 570-571 (1966). The second, or "bad act," requirement ordinarily involves an effort by the monopolist to deter or prevent entry by a competitor. See, e.g., Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 105 S.Ct 2847 (1985). This requirement would not, however, be satisfied merely by charging monopoly rates to shippers. See Berkey Photo Inc. v. Eastman Kodak Co., 603 F.2d 263 (2d Cir. 1979), cert denied, 444 U.S. 1093 (1980).

Where a violation of the antitrust laws has been established, injured parties may recover three times their damages plus costs of the lawsuit, including reasonable attorneys' fees; injunctive relief also may be available. Both legal and equitable relief are subject to the limitations in Keogh and section 16 of the Clayton Act, as noted in the response to Question 2 above.

4. If the ICC exempts particular bulk commodities from maximum rate regulation under 49 U.S.C. § 10505, what remedies does the shipper have under the Staggers Act if a monopoly carrier imposes unreasonable rates?

A. If the ICC were to exempt specific bulk commodities from maximum rate regulation, but from no other provisions of the Interstate Commerce Act, then the other remedies described in the response to Question 1 above would still be available in appropriate circumstances.

5. Does the availability of a remedy under the Staggers Act foreclose remedies under the antitrust laws?

A. As a general proposition, the existence of possible regulatory remedies under the Staggers Act does not foreclose the availability of antitrust remedies for complaints based on the same underlying situation or conduct. However, under the doctrines of primary and exclusive jurisdiction, antitrust courts do defer to regulatory agencies in cases where antitrust enforcement would interfere with a lawful order of a regulatory agency, or would inevitably intrude upon the agency's prerogatives and jurisdiction. For example, antitrust suits against proposed railroad mergers are foreclosed by the ICC's primary and exclusive jurisdiction over such transactions. 49 U.S.C. 11341. On the other hand, implied repeals of the antitrust laws are disfavored and found only in cases of "plain repugnancy between the antitrust and regulatory provisions." United States v. Philadelphia National Bank, 374 U.S. 321, 350 (1963). Accordingly, the mere existence of maximum rate regulation as a remedy at the ICC, or of the ICC's authority to impose reciprocal switching, would not automatically require a court to deny antitrust relief in cases where a rail carrier is shown unlawfully to have monopolized a rail transportation market.

6. Mr. Palmer of Western Fuels Association and Mr. McKeever of Western Coal Development both testified on April 22, 1985 that Keogh v. Chicago & Northwestern Rail Co., 260 U.S. 156 (1922) immunizes railroads from antitrust damages for using monopoly power to set unreasonable rates. Are they correct?

A. Keogh held that where the ICC had approved as reasonable and non-discriminatory rates filed by a group of carriers, a shipper could not recover damages in an antitrust action even if the rates resulted from a conspiracy among the carriers to fix prices. Under the holding in Keogh, a private antitrust plaintiff is precluded from attempting to establish that a particular rate is unreasonable if the ICC has determined that it is reasonable. The Supreme Court recently granted a petition for a writ of certiorari in Square D Co. v. Niagara Frontier Tariff Bureau, Inc., 760 F.2d 1347 (2d Cir. 1985), cert. granted, 54 U.S.L.W. 3193 (Oct. 7, 1985), a case in which the United States filed a memorandum, as amicus curiae, urging the Court to grant the writ and reexamine Keogh. On November 21, 1985, the Solicitor General filed a brief for the United States on the merits in Square D, a copy of which is enclosed. In that brief, we argue that Keogh should be overruled.

7. Does Keogh bar an antitrust damage action if monopoly carriers are subject to maximum rate regulation under the Staggers Act?

A. The Department believes that where the ICC's jurisdiction extends only to prescribing maximum rates that carriers may charge, and carriers thus are free to set rates anywhere below the maximum, Keogh should not be held to bar a private antitrust action for damages. The Seventh Circuit, however, recently held that Keogh does bar private damage actions even where the ICC does not have the authority to prescribe maximum rates. In re Wheat Rail Freight Rate Antitrust Litigation, 759 F.2d 1305 (7th Cir. 1985). If the Supreme Court adopts our position in Square D (see answer to question 6, above), this holding of the Seventh Circuit would have to be reexamined by that court in light of the Supreme Court's decision in Square D.

8. Does it apply if such carriers have been exempt under 49 U.S.C. § 10505?

A. 49 U.S.C. 10505 provides that the ICC "shall exempt a person, class of persons, or a transaction or service when the Commission finds that the application [of the Interstate Commerce Act] is not necessary to carry out [national] transportation policy . . . and . . . not needed to protect shippers from the abuse of market power." If the ICC were to determine that a carrier should be wholly exempt from regulation under this section, the rationale of Keogh would be inapplicable because of the absence of rate regulation and Keogh would not bar an antitrust action for damages.

9. Assuming that captive shippers have antitrust remedies for damages against a monopoly carrier, how is this remedy a practical constraint against abuse under current interpretations of § 2 of the Sherman Act?

A. In situations where Keogh would not bar money damage recoveries by a shipper, the threat of treble damages would have the same deterrent effect to violations of section 2 of the Sherman Act that it has in other industries. As in other industries, of course, the Sherman Act does not make it illegal to possess lawfully-acquired monopoly power or to charge monopolistic prices. As mentioned in the response to Question 3 above, unless there are "bad acts" of monopolization, section 2 is not violated, and treble damage or other antitrust relief is not available.

10. Has the Antitrust Division received any complaints from captive shippers complaining of unfair treatment by sole access rail carriers?

A. Yes.

11. Has the Antitrust Division conducted any systematic economic studies or investigations of the captive shipper problem in response to such complaints or otherwise?

A. Whenever the Antitrust Division receives a complaint, it first determines whether the antitrust laws may have been violated. If there is reason to believe an antitrust violation has occurred, the Division makes a further determination whether the complaint is an appropriate one for public antitrust enforcement by the federal government as opposed to private or local enforcement. Complaints are investigated on a case-by-case basis and no systematic economic studies of "the captive shipper problem" have been undertaken. To date, the Department has not identified a captive shipper situation that merits formal enforcement action.

12. If the answer to question 11 is no, what is the basis for your testimony that there is no captive shipper problem?

    A. The Department has not concluded that there is no captive shipper problem. There is, however, no evidence of a problem that requires legislation along the lines of S. 447.

13. Why would this bill impose greater burdens on the courts as you have testified (n.1), than currently applicable law under section 2 of the Sherman Act?

    A. The bill would substantially increase the burden on the courts for two reasons. First, more cases would be filed because no showing of monopoly power would be required; instead, every shipper served by only one railroad--a common situation--would be given a cause of action. Second, for those cases that are filed, the bill provides for complex regulatory-type relief that federal district judges are not well-equipped to handle. Each federal district court would be asked to administer, on its own, the types of remedies that regulatory agencies currently impose and monitor on an industry-wide basis.

14. Does the source competition that you describe at p. 4 of your testimony constrain carriers from appropriating economic rents as between themselves and captive shippers?

    A. It is possible that even when source competition prevents a shipper or its railroad from being able to affect a product's price at a destination, the shipper and railroad can still earn economic rents on shipments of that product to that destination. As in any market, including highly competitive ones, such a result will occur when firms' costs of producing and delivering the product are lower than their competitors' costs. The division of these rents between shipper and railroad will depend on the agreement between those parties. While that division will affect the relative position of each party, it will not affect overall economic welfare because the division will not affect the delivered price.

15. What is the factual basis for your statement that shippers with captive facilities on different railroads may be able to "play the railroads off against one another" (p. 4-5)?

A. The Department's experience has shown that this phenomenon occurs with grain shippers in the Midwest and may occur with other shippers as well. For example, a large grain cooperative that has several storage facilities in the same general area but located on different railroads' lines can increase or decrease its shipments to and from its locations in response to terms offered by the different railroads serving those various locations.

16. Do you have any systematic statistical basis for your statements (p.5) concerning intermodal competition? Would you supply this data, if any, to the Committee?

A. The Department has studied the effectiveness of intermodal competition as part of its investigations of the competitive effects of several railroad mergers. The results of these studies are contained in verified statements that the Department has submitted to the ICC in its proceedings involving these mergers, and in the Department's correspondence with the Secretary of Transportation and Congress concerning the proposed acquisition of Conrail by Norfolk Southern. These statements, which assess the role of intermodal competition in many different instances involving specific commodities and locations, are based on data from the 1977 Census of Transportation, on data from Reebie Associates, a private consulting firm, and on a large number of interviews with shippers. The strength of intermodal competition varies widely, depending on many factors, including the characteristics of the commodity involved, the distance it must be transported, and the availability of alternative modes. While in many cases intermodal competition has little, if any, effect on a railroad's ability to set prices, in many other cases such competition will prevent a railroad from exercising market power.

17. If, as you testified at p. 6, the standard of liability in S. 447 falls short of proving monopoly power and the presence of a competitive problem, are the "abuse of power" and "absence of effective" competition standards in §§ 10101(a)(b) and 10505(a)(2)(B) similarly defective?

A. The Department's objections to S. 447 include the fact that there is no competition standard in the bill, such that liability could be imposed even in highly competitive situations. In contrast, the existing statutory phrases "abuse of market power" and "absence of effective competition," while not necessarily wholly congruent with the standards of unlawful monopolization that have evolved under section 2 of the Sherman Act, clearly contemplate anticompetitive situations and conduct.

18. If, as you testify (p. 6), the "essential facilities" doctrine "has proven difficult to apply in practice," do shippers have a meaningful antitrust remedy based upon it?

A. Two major problems have been encountered in applying the essential facility doctrine. First, it can be difficult to identify what facilities actually are essential. In particular, the court must determine whether plaintiffs could duplicate the facility within a given length of time and whether the time required to duplicate it would be long enough to give its owner significant monopoly power.

Second, the court must set a price for use of the facility that allows the facility owner to earn a competitive rate of return. Setting the proper price requires the court to assess a number of complex factors, including the risk of the investment in the facility, the cost of operating it, and the extent to which its value depreciates over time. If the court sets too high a price, the owner will continue to earn monopoly profits. If the court sets too low a price, the owner will not be able to earn a competitive rate of return and will then be unwilling to invest in maintaining the facility; thus, the facility eventually will deteriorate, to the detriment of consumers.

The Department certainly does not deny that the "essential facility" doctrine is part of antitrust law, or that shippers or others may obtain relief under that doctrine. However, given the serious difficulties inherent in applying the doctrine, we believe that it should be reserved for those cases where the competitive harm is clear and no other effective remedy is available.

19. Is a monopoly railroad entitled to a greater return on its investment than it could earn from competitive pricing?

A. Under a rate regulation regime, a monopoly railroad ideally should be permitted to charge prices that yield a competitive rate of return on its investment, but no more.

20. If not, what adverse results in the market place follow from applying the "essential facilities" doctrine subject to the limits of 49 U.S.C. § 10101(a)(6)?

A. Whenever the essential facility doctrine is invoked, there is a serious risk that the court will set a price for use of the facility that is either too high or too low, with the results discussed in our response to Question 18 above.

21. Why do you assume (p. 7) that a court will find rates equivalent to those set by competitive forces to be unreasonable?

A. One of the Department's objections to S. 447 is that the bill would create a right of action even when trackage rights or other access fees are set by competitive market forces. The sole criterion for establishing a right to relief under S. 447 is whether the shipper has direct access to only one rail carrier. Where access fees are in fact competitively determined, any suit instituted pursuant to S. 447 necessarily would involve an allegation by the plaintiff that the access fee was nonetheless unreasonably high. The court then would have to do one of two things. It could find for the defendant railroad, in which case the right of action created by S. 447 would result in wasted litigation costs. Alternatively, the court could find for the plaintiff and lower the competitively-determined access fees currently being charged; in that case, the bill plainly would have a negative and pernicious economic impact in the market. It is important to remember, moreover, that it is no easy task for a court to determine whether a rate is "competitive" or not. One cannot expect the courts to do a very good job in outguessing the market, particularly where they are not required to determine that competitive market conditions do not exist before establishing rates.

22. If S. 447 were revised to refer the rate issues to the ICC under the primary jurisdiction doctrine, would your concern about judicial disparity in rate determinations be alleviated?

A. In the Department's view, S. 447 presents no issues that are not "rate issues," other than the easily-determined ones whether a railroad provides sole access to a shipper and whether the commodity involved is covered by the bill. But if all "rate issues" were automatically referred to the ICC, there would be no reason to involve the courts (except in their traditional role as appellate reviewers of administrative decisions). Thus, if S. 447 were revised simply to amend the Interstate Commerce Act rather than the Sherman Act, our concerns about disparity in judicial rate determinations would be largely alleviated. However, as we have indicated, we believe that the amendment of the Interstate Commerce Act embodied in the Staggers Act provides an adequate statutory basis for resolving the captive shipper problem. No further amendment is required.

23. Since, as you testify, the Department of Justice does not monitor the ICC's market dominance and reciprocal switching cases, on what basis do you address the issue of trackage rights?

A. Our testimony stated that the Department does not normally monitor the factual records in market dominance and reciprocal switching proceedings. The Department addressed the issue of trackage rights only to point out that market distortions will occur unless trackage rights rental rates cover the true cost of providing access to a second carrier. If the rental is set too low, investment in track will decrease and the service to the shipper will deteriorate, regardless of the particular facts involved in a shipper's complaint.

24. The ICC has invited comments in Ex Parte 445 (Sub. No. 1), Intramodal Rail Competition, 50 Fed. Reg. 13051 (April 2, 1985). You state in your testimony (p. 10) that the Department is "currently studying the proposal." Does the Department intend to file comments and is the Department aware of when the ICC rulemaking will be finished?

A. The Commission served a decision in this proceeding on October 31, 1985, adopting rules designed to assist captive shippers. The Department did not file comments in Ex Parte 445, but we have no objection to the rules as adopted. See our answer to supplemental question 5 below.

25. How long should Congress wait for the ICC to issue a rule in Ex Parte 445 (Sub. No. 1)?

A. See the answer to question 24 above.

26. Given the regulatory history of the terms "reasonable" and "fair return," why do you assume they are vague?

A. The terms "reasonable" and "fair" are inherently vague, and their vagueness is not significantly alleviated by the fact that the ICC and other regulatory agencies have long grappled with the terms. If anything, the regulatory history of these terms demonstrates the disparity with which they can be applied to similar competitive situations. Moreover, the vagueness of the terms is exacerbated by the difficulty of measuring the true economic costs of providing rail service and of allocating those costs to particular traffic.

27. Please furnish the Committee all communications with the ICC or anyone outside the Department of Justice concerning your testimony.

A. To our knowledge, prior to our testimony on S. 447 no one at the Department communicated with anyone outside the Department about that testimony, except for communications with the Office of Management and Budget during the usual clearance process. In particular, no one at the Department contacted anyone at the ICC about our testimony.

28. Are there any amendments you would suggest to this Committee that would improve the application of the antitrust laws as they relate to railroads.

A. No. As noted above in our response to questions 6 and 7, however, the Department believes that the Keogh rule should be overturned by the Supreme Court. Such a result would strengthen the application of the antitrust laws to industries in which tariffs are filed, including the railroad industry.

29. Recent developments in the long distance telephone market as a result of the MCI case have precluded AT&T from extending its local monopoly into the long distance market. Has this been in the public interest?

A. The Modification of Final Judgment ("MFJ") in United States v. Western Electric Co., 552 F. Supp. 131 (D.D.C. 1982), which resulted in the divestiture by AT&T of its local operating companies, was found by the judgment court to be in the public interest. Prior to the MFJ, AT&T had been extensively regulated for years because of its monopoly power in local telephone markets and its dominant position in the provision of long distance telephone service and the manufacture of telecommunications equipment. Indeed, AT&T's integrated structure was deemed to require comprehensive federal regulatory intervention in markets that otherwise would have been shaped solely by free market forces.

The 1982 settlement of the Department's antitrust suit against AT&T was designed to separate AT&T's regulated businesses (the seven regional Bell operating companies (BOCs)) from businesses that were, or could be, unregulated (AT&T). Once separated from the telephone system's regulated bottleneck functions (the local exchange networks), the remainder of AT&T, including the long distance and manufacturing businesses, would be free to enter all businesses. Thus, the MFJ was designed both to deregulate much of AT&T and to ensure that the divested BOCs would not be able to use their position as government-protected monopolists to thwart competition and efficiency in markets that otherwise could sustain competition and a free market approach. The AT&T divestiture was accomplished solely under the existing antitrust laws and did not require new legislation of a type analogous to S. 447.

30. Doesn't the same principle apply here? Haven't the railroads used their local monopoly to foreclose competition in long distance rail transportation?

A. As discussed above, the Department does not normally monitor specific factual situations that are involved in ICC market dominance or reciprocal switching cases. Accordingly, we have no basis for determining whether, in any given case, a railroad may have used its monopoly access to a captive shipper to "foreclose competition in long distance rail transportation." It should not be assumed, however, that all refusals to switch or all joint rate cancellations represent the exercise of monopoly power over a captive shipper. Indeed, the Department's long experience with the railroad industry has led us to conclude that most such actions do not represent the exercise of monopoly power.

Even as a theoretical matter, caution should be used in applying this analogy. In particular, unless the "local" rail rate is regulated or otherwise constrained, the analogy is inappropriate. As long as a rail carrier is free to charge whatever it wants for the access it controls, it will have little or no incentive to prevent the longhaul service from being provided by the most efficient competitors. Moreover, unlike S.447, the MFJ does not require the courts to set rates for telecommunication services.

31. Do you agree that railroad deregulation should be coupled with a general strengthening of the application of the antitrust laws to railroads?

A. Deregulation of any industry inevitably leads to a general strengthening of the application of the antitrust laws to that industry. This is true simply because the limited antitrust immunities that regulated industries enjoy are a result of the regulation. When the regulation is removed, the rationale for the antitrust exemption is likewise removed, and the antitrust laws then apply more fully to the deregulated industry. New legislation, such as S. 447, thus is not necessary to strengthen the application of the antitrust laws to railroads as they become increasingly deregulated.

32. Do you agree with the proposition that competition, rather than regulation, leads to most efficient and economic use of the nation's resources?

A. Yes.

33. Isn't it true that the Department of Justice has advocated before courts of appeal that Keogh should no longer be the law, given the changed regulatory environment?

A. Yes. In In re Wheat Rail Freight Rate Antitrust Litigation, 759 F.2d 1305 (7th Cir. 1985), the Department argued that where the ICC has no authority to review whether a particular rate is reasonable, Keogh should not be held to bar a damage action based on the failure of rail carriers to comply with the notice and hearing requirements of a collective ratemaking agreement approved by the ICC pursuant to 49 U.S.C. 10706. See our answers to questions 6 and 7 above.

34. What is Justice's position on Keogh?

A. As noted above in our answer to question 6, the Keogh issue is now before the Supreme Court in the Square D case, and the Department has urged the Court to overrule Keogh.

As long as Keogh remains good law, the Department believes that whether the doctrine bars a private damage action in a particular case depends on the extent of the ICC's regulatory authority over the conduct at issue, and on whether the imposition of treble damage liability would frustrate the ICC's ability to discharge its regulatory responsibilities under the Interstate Commerce Act.

35. Does the refusal of the Southern Pacific to allow the Union Pacific to cross 980 ft. of railyard to serve the new GM/Toyota plant in California constitute monopolization? If so what are Union Pacific's remedies? Are not those remedies enhanced by the provisions of S. 447?

A. According to papers filed at the ICC on May 20, 1985, an agreement has been reached whereby Southern Pacific ("SP") will switch cars for Union Pacific ("UP") at the GM/Toyota plant. Thus, it appears that what the question characterizes as a "refusal of the [SP]" may have been no more than a contract dispute between the parties. Unless the agreed switching rates reflect monopoly profits for SP, there is no competitive problem to be addressed by the ICC.

Even if the dispute still existed, however, in order to prevail in a Sherman Act suit UP would have to establish that the rail transportation of GM/Toyota cars from the plant to one or more specified destinations constitutes a relevant market in which SP exercised monopoly power. UP also would have to prove that SP's alleged refusal to grant a right of way was intended unlawfully to achieve or maintain that power rather than an act justified by legitimate business concerns. If UP could thereby prove unlawful monopolization, then S. 447 might enhance the remedies available under current law in two respects. First, S. 447 would make it clear that a private party can obtain injunctive relief against a regulated rail carrier for violations of the Sherman Act. Second, S. 447 would remove Keogh as an issue in situations where it might arguably apply. The problem with S. 447, however, is that UP might be able to obtain relief even though the rail rates for the movement of cars from the plant were constrained by competitive market forces, and even though SP had valid and procompetitive or competitively neutral business reasons for refusing access.

ANSWERS TO SUPPLEMENTAL QUESTIONS

1. Mr. Rule, at p. 2 of your statement you state that regulatory provisions of S. 447 would "prevent railroads from earning competitive rates of return." If the bill were modified so that it only prevented railroads from earning supra competitive rates of return on various lines of traffic, would your objections to the bill remain? And if so, would you please explain why?

   A. The proposed change would not alter the Department's objection to the bill. Whether the operative language of the bill is "unreasonable rate of return," "fair rate of return," or the proposed "supracompetitive rate of return," the bill would continue to be a regulatory provision to be administered by the courts on a case-by-case basis. Courts would still be required to set trackage rights fees or joint rates under inherently vague standards, and would still be required to do so in situations where there may be no competitive problem.

2. Mr. Rule, would you assume for a moment that section 9(a)3 of the bill is removed and that there are no "regulatory" provisions left, only antitrust provisions designed to apply the essential facilities doctrine to the railroad industry. If that situation were to exist, would it not be a fact that the bill only would apply to permit entry to an essential facility where there were no factors otherwise restraining price? Stated differently, in a highly competitive market with competitive prices being charged, the likelihood of a shipper seeking entry into that market would be extremely unlikely. Would you agree?

   A. The Department would not agree. First, section 9(a)3 is not the only "regulatory" provision of the bill. Sections 9(a)1 and 9(a)2 are also regulatory because they would place the issue of reasonableness of access fees before the courts, to be determined "in accordance with generally accepted principles regarding just and reasonable rental of track."

   Second, the essential facility remedy--"non-discriminatory access on fair and reasonable terms"--is not a typical antitrust remedy awarding damages or enjoining specific conduct, but is in fact a quasi-regulatory remedy to be fashioned and enforced by the courts. As discussed above, the essential facility doctrine is difficult to apply in practice because of its regulatory nature, and it has been applied only where the competitive problem is clear and no other effective remedy is possible. The doctrine is best applied only in simple situations, such as those involving switching or trackage that is not also used to handle a significant volume of non-captive traffic.

Third, even assuming that the foregoing problems could be avoided, a bill--like S. 447--that makes the essential facility doctrine available in competitive situations is not benign. In our view, a shipper's willingness to litigate under this section would not likely depend on whether the rate the shipper currently is receiving is competitive; rather, it would depend on whether the rate it might obtain as a result of litigation was sufficiently below the current rate to justify the risk and cost of litigation. Moreover, a court could mistakenly order access at a fee that failed to compensate the track-owning railroad for the cost of allowing second carrier access, thus resulting in disinvestment in and deterioration of the essential facility.

3. **Mr. Rule, I would like you to explain your statement on p. 6 that "even the essential facility doctrine which requires a showing of monopoly power, has proven difficult to apply in practice and can be critized as denying the facility owner a legitimate return on its investment." Are you suggesting, sir, that the MCI and Otter Tail decisions are wrong and that the essential facilities doctrine should be repealed legislatively or overturned judicially?**

A. The Department does not disagree with the decisions in the MCI or Otter Tail cases, although neither case required the court to regulate access fees to an essential facility. The MCI case (MCI Communications Corp. v. AT&T, 708 F.2d 1081 (7th Cir.), cert. denied, 104 S. Ct. 234 (1983)), involved only damages for a denial of access, and in Otter Tail (Otter Tail Power Co. v. United States, 410 U.S. 366, 375 (1973)), the court ordered that the defendant wheel power only "at rates which are compensatory and under terms and conditions which are filed with and subject to approval by the Federal Power Commission." In both cases, therefore, the courts properly avoided the difficult rate regulation issues, leaving them to agencies that were better equipped to handle them.

4. Mr. Rule, you testified at the April 23, 1985 hearing on S. 447 that no new legislation is required to protect captive shippers and carriers allegedly injured by anticompetitive railroad actions because adequate remedies exist in the Interstate Commerce Act and the current antitrust laws. In view of this position, would you please review the following summaries of ICC cases dealing with competitive access issues and address the questions following these descriptions.

A. Joint Line Cancellation--Soda Ash--UP R. Co., 365 I.C.C. 951 (1982). In this case the Commission discontinued its suspension and investigation of joint rate cancellations by Union Pacific Railroad (UP). The UP had cancelled joint rates with the Ann Arbor Railway System on soda ash movements in which the Ann Arbor participated as a bridge carrier in competition with UP's preferred routings. While both carriers had access to particular gateways, only the UP served the relevant origins. The Ann Arbor previously had flagged out of a general rate increase, enabling the movement in which it participated via joint rate with UP to compete more favorably with UP's preferred routes. The UP responded by cancelling its joint rates with the Ann Arbor, although it was still making a profit on those joint routes even with the cap caused by the Ann Arbor flag-out.

The Commission permitted the UP cancellations to become effective, holding that because the cancellations eliminated inefficient, circuitous, joint route movements, this conclusively established that the UP's actions contributed to sound economic conditions and, thus, were consistent with the national Rail Transportation Policy. 365 I.C.C. at 970.

QUESTION: (1).

Is the Commission's position a correct interpretation of the Interstate Commerce Act and, if so, how does this square with the Antitrust Division's position that the Interstate Commerce Act provides adequate protection against anticompetitive railroad conduct?

(2).

Would you anticipate that the Ann Arbor Railway would have any greater success had it filed a complaint pursuant to Section 2 of the Sherman Act? Please explain your answer.

B. Interchange Provisions at Jacksonville, FL, SCL and SRS, 365 I.C.C. 905 (1982). In this case the Commission discontinued its investigation of joint route and joint rate cancellations by Seaboard System Railroad on SFA intraterritorial movements between Seaboard and Southern Railway local stations that included an interchange at Jacksonville, Florida. The tariff was protested by the Southern Railway and numerous shippers.

The Seaboard tariff had a particularly adverse impact on bulk commodity shippers located in Florida's Bone Valley. These shippers are captive to Seaboard for rail transportation, and other modes are inadequate substitutes. Prior to Seaboard's joint route cancellations, these shippers were able to negate significantly Seaboard's market power at their origins due to the availability of an interchange of traffic between Seaboard and Southern at Jacksonville. This interchange gave Southern a long-haul movement to SFA destinations local to that carrier; in addition, shippers were provided competitive alternatives to other movements in which Seaboard obtained a substantially longer haul by interchanging with Southern north of Jacksonville.

Rather than continue to compete for this traffic, the Seaboard chose instead to gain its long-haul by refusing to interchange with Southern at Jacksonville. The tariff publication enabled Seaboard to extend its monopoly power at origin to the line-haul movement. As a result, shippers lost the ability to choose among transporation alternatives and Southern was arbitrarily eliminated as a competitor.

The Commission discontinued its investigation of Seaboard's tariff publication, holding that the cancellation was consistent with the public intererst since the remaining Seaboard long-haul routes were less circuitous and more efficient.

QUESTION: (1).

Is the Commission's position a correct interpretation of the Interstate Commerce Act and, if so, how does this square with the Antitrust Division's position that the Interstate Commerce Act provides adequate protection against anticompetitive railroad conduct?

(2).

Would you expect the Southern Railway and/or a shipper in the Bone Valley to succeed in these circumstances if a complaint had been filed against the Seaboard pursuant to Section 2 of the Sherman Act? Please explain your answer.

C. Docket No. 38891, Central States Enterprises, Inc. v. Seaboard Coast Line Railroad Company, et al., (not printed) served May 15, 1984, petition for review pending, 7th Circuit, filed June 15, 1984). In Central States a grain shipper sought a reciprocal switching arrangement for its grain elevator at Camilla, Georgia. The elevator is served exclusively by the Seaboard System Railroad. The complainant desired to ship grain single system on the Norfolk Southern from Fort Wayne, Indiana to Camilla, with Seaboard performing reciprocal switching at destination. The Seaboard cancelled N&W-SBD joint rates that had competed with the Norfolk Southern single system route. The obvious purpose of Seaboard's action was to force the shipper to transport grain to Camilla single line on the Seaboard from origins other than Fort Wayne. The Norfolk Southern single system movement was hampered by the fact that the Southern served Camilla but only the Seaboard physically served the complainant's facility. Yet, because the transporation charges were cheaper in comparision to the alternative Seaboard single line routes, the shipper transported the grain on the Norfolk Southern from Fort Wayne and trucked it across town to the grain elevator once the Southern reached Camilla. The shipper sought reciprocal switching to ensure that grain would continue to move from its Fort Wayne elevator, where it could purchase grain in very high volumes for sale to the feed and export industries. All-rail service from Fort Wayne was necessary for the complainant to remain competitive in the sale of feed grain to the poultry and livestock markets in the south.

The Commission denied complainant's relief primarily on two grounds. First, the Commission ruled that reciprocal switching could not be ordered because the grain elevator was located outside of Seaboard's switching limits for Camilla. Second--and in an "even if" type argument-- the ICC held that a reciprocal switching agreement was not required since Seaboard was revenue inadequate.

QUESTION: (1).

You specifically mentioned in your testimony that section 11103(c) of the Interstate Commerce Act, 49 U.S.C. § 11103(c), is an adequate remedy for a captive shipper. Do you believe that the Commission correctly interpreted that section, particularly its apparent position that reciprocal switching arrangements should not be required where the would-be switching railroad is revenue inadequate?

(2).

Do you believe that the complainant would have succeeded in an antitrust lawsuit filed against Seaboard pursuant to section 2 of the Sherman Act? Please explain your answer.

A. This question seeks the Department's views on three ICC proceedings involving "competitive access issues". The first two cases involved joint rate cancellations and the third involved a refusal to switch reciprocally. In particular, the question seeks the Department's view as to whether the Interstate Commerce Act was correctly interpreted in each case, and whether and how the results might have been different had the cases been brought under section 2 of the Sherman Act.

While the Department is happy to comment generally on the competitive implications of refusals to interchange, we hesitate to second-guess the ICC's interpretation and application of its own statute to particular facts. The courts of appeals, of course, give great deference to an agency's decision in these circumstances. That policy is especially justified here, since the standards that determine whether joint rate cancellations are lawful are broad and not restricted to competitive considerations. Similarly, the ICC has broad discretion in deciding whether to order reciprocal switching. Thus, while the Department believes the Interstate Commerce Act usually provides adequate remedies for captive shippers, including remedies that are not available under the antitrust laws, the Act does not (and should not) guarantee that shippers will always prevail in their disputes with carriers. Much is properly committed to the sound discretion of the Commission.

We are similarly cautious in predicting the outcome of hypothetical section 2 cases based on the limited facts available. Section 2 of the Sherman Act does not always lend itself to confident predictions of litigation success or failure, even where the Department has conducted a thorough factual investigation. However, in responding to your questions we will comment on any clear differences between the ICC regulatory proceedings cited in your question and hypothetical antitrust cases based on the same facts.

Before addressing the cases individually, we wish to emphasize several points that apply to a competitive analysis of all such cases, regardless of the forum in which relief is sought:

1. A railroad's refusal to interchange traffic, whether by refusing to grant reciprocal switching or by refusing to participate in a through route, is an example of what antitrust law refers to as a vertical restraint. For example, when a railroad refuses to grant reciprocal

switching it essentially is forcing shippers who purchase its switching services also to purchase its linehaul service. That refusal is a form of tying arrangement, i.e., a requirement that in order to purchase one product or service a purchaser must also purchase a second product or service. The Department has recognized that while vertical restraints often have procompetitive effects, they can have anticompetitive effects in certain circumstances. See U.S. Dept. of Justice, Vertical Restraint Guidelines (January 23, 1985). This situation prevails in the railroad industry as in other industries.

2. Refusals to interchange by railroads without market power over a particular movement are not anticompetitive; to the contrary, they simply represent a carrier's decision to withdraw from a non-remunerative or inefficient joint venture. Restricting such refusals does not increase competition among railroads, but it does tend inefficiently to freeze existing contractual relationships among railroads, and forces a carrier to accept a less-than-competitive return.

3. Cancellations by carriers with market power over a movement can be anticompetitive in some circumstances, however. One situation where a joint rate cancellation by a rail carrier with market power over a captive shipper might be anticompetitive exists when the the rail carrier's freedom to charge monopoly prices over its sole access rail link is constrained. For example, if a rail carrier's ability to price freely on its sole access rail link is constrained by direct regulation (see U.S. Dept. of Justice, Merger Guidelines (June 14, 1984), § 4.23), by the perceived threat of regulation, or by pre-existing joint rates or reciprocal switching, the carrier may require a captive shipper to use its long haul. By cancelling alternative longhaul routings, the originating (or terminating) carrier can capture monopoly profits on the full unregulated or unconstrained movement that it cannot achieve on the monopoly link alone.

4. Another situation where a joint rate cancellation might be anticompetitive exists where the cancellation tends to exclude rivals from rail markets. See Vertical Restraints Guidelines, supra, § 3.22. In the rail industry, this possibility is illustrated by a situation where railroad 1 has a monopoly link between points A and B, but competes with railroad 2 between points B and C. Traffic going from A to C may travel solely on railroad 1 or it may be interchanged with railroad 2 at B. A railroad's cost of hauling an additional unit of traffic usually increases as the volume of traffic on its lines decreases. Thus, if railroad 1 can prevent railroad 2 from receiving any traffic originated at A, then railroad 2's cost of hauling additional traffic from B to C may increase. As a result, railroad 2 may have to raise its price for B/C traffic. Thus railroad 2 will be a weaker competitor for railroad 1 in the market for B/C traffic. In this situation, the market where the anticompetitive effect may occur (B/C) is not the market in which the cancellation occurs (A/B). For the diversion of traffic by railroad 1 from 2 to be anticompetitive, it must result from railroad 1's pursuit of monopoly profits in market B/C rather from the lower prices or better service derived from railroad 1's superior efficiency in market A/C.

5. The prohibition of joint rate cancellations is indirect maximum rate regulation. A rail carrier's monopoly profits on any movement are limited to those yielded by its division of the least profitable joint rate in which it is required to participate. (Similarly, a carrier's monopoly profits are limited to those yielded by switching it is required to perform.) Any further profits it might earn on the movement will be constrained by competition from other railroads. If competition were the standard for judging a joint rate cancellation, the only issue would be whether the cancelling carrier has market power over the movement in question. If so, the

cancellation should be prohibited only if the current division of the joint rate allows the cancelling carrier to earn at least a competitive rate of return, but constrains the carrier's exercise of market power and therefore enhances welfare. This inquiry is necessary because, due to the existence of inefficient routes, a rail carrier with market power may still earn less than competitive returns on some of its joint rate divisions.

With these points in mind, we turn to a discussion of the three ICC cases cited in your question.

A. Joint Line Cancellation - Soda Ash - UP R. Co., 365 ICC 951 (1982). In this case, the ICC upheld joint rate cancellations by Union Pacific Railroad ("UP") involving soda ash movements in conjunction with the Ann Arbor Railway System. According to the ICC findings, soda ash is used in the manufacture of glass, pulp, paper, soap and detergent. In most cases, it is an indispensible material, and 83% of the total in 1979 was produced in mines captive to the UP. Thus, soda ash shippers appear to have the characteristics of captive shippers over whom the UP could exercise monopoly power through its exclusive access. However, we cannot conclude from the facts presented that UP would have violated the Sherman Act.

The dispute originated when the Ann Arbor "flagged out of" (i.e., declined to participate in) a seven percent general increase approved by the Commission in Ex Parte 357 on December 15, 1978. An anomaly in the regulatory process prevented any of the participating carriers in a route involving Ann Arbor from raising their rates. As a result, the lower rate applied not only to Ann Arbor, but to all other carriers in the movement, including UP, even though they may have desired to implement the general rate increase. Accordingly, the "competitive" route that Ann Arbor was able to create was not solely a result of its own initiative, but rather was a result of Ann Arbor using the regulatory system to require the participation of other carriers, including UP, on terms they did not desire.

There was no evidence that UP was evading the regulation of its soda ash rates or that it was depriving Ann Arbor of overhead traffic in order to gain an advantage in markets where they were direct competitors; indeed, Ann Arbor and UP were not direct competitors at any point. At most, therefore, the Ann Arbor action might possibly have constrained UP's ability to charge a monopoly price for its soda ash movements. Moreover, since Ann Arbor's interference with UP's pricing freedom was the result of a quirk in the regulatory system, UP's withdrawal from joint rates under those circumstances might have been a justifiable response in this peculiar regulatory context. Under these circumstances, it is not at all clear that the joint rate cancellations would support a claim of unlawful monopolization.

B. Interchange Provisions at Jacksonville, Fl, SCL and SRS, 365 ICC 905 (1982). This case involved cancellations by Seaboard Coast Line ("SCL") of certain joint rates with Southern Railway over Jacksonville, Florida. The ICC's decision does not specify what commodities were involved, but the Department is aware that the overwhelming majority of all phosphate produced in the United States is mined in the Bone Valley area of Florida, is captive to SCL, and generally is not truck-competitive.

There is little in the ICC's factual summary from which to conclude that SCL possesses monopoly power over phosphate shippers or that the cancellation of joint rates for phosphates was anticompetitive. Unlike the soda ash case, there was no evidence that the cancelled routing offered lower rates. As in the soda ash case, there was no evidence of regulatory evasion by SCL and no evidence that SCL sought to deprive Southern of overhead traffic in order to gain an advantage on routes where the carriers are direct competitors.

The only argument advanced that the cancellations were anticompetitive was that the elimination of an alternative route removed the shippers' ability to threaten to short-haul SCL (or Southern), an ability that allegedly gives shippers some leverage over rates and service. As an abstract matter, if SCL had market power over the movement but was required by regulation to participate in the joint rate it wished to cancel, then SCL would indeed have to take competitive steps, such as lowering the rate on its long-haul, to make its preferred route more attractive to shippers. The ICC found, however, that this argument was not supported by the evidence in this case, see 365 ICC at 915, and the Department cannot say that that the agency's factual determination was clearly erroneous.

C. Docket No. 38891, Central States Enterprises, Inc. v. Seaboard Coast Line RR. Co., decision served May 15, 1984. This case involved the ICC's refusal (Chairman Taylor dissenting) to order SCL to switch inbound cars from Southern Railway to a grain elevator located just outside of the Camilla, Georgia switching district. Southern and SCL perform reciprocal switching for each other within the Camilla district, and Central States petitioned to have its elevators, which are served exclusively by SCL, included in the reciprocal switching service. With reciprocal switching, Central States could receive direct rail shipments on Southern as well as on SCL.

As noted above, the ICC has broad discretion in deciding whether to exercise its permissive authority under section 11103(c). The Department has disagreed with particular ICC reciprocal switching decisions in the past (see Protest of the Department of Justice, Reciprocal Switching on Chessie System Railroads, Case No. 71002, Feb. 11, 1983). Such disagreements reflect our view that Congress intended the Staggers Act to mandate maximum intramodal competition where feasible, and that refusals to switch undermine that goal. We believe that is why Congress included section 11103(c) in the Staggers Act; that section recognizes the important distinction between regulation of short railroad spurs used to serve only captive shippers and regulation involving linehaul track used to serve competitive traffic.

Nonetheless, the ICC's decision in Central States is within the bounds of the agency's permissible discretion under the Interstate Commerce Act. In particular, while the ICC is not required to consider revenue adequacy when deciding whether to act in switching cases, it is not prohibited from doing so. However, under the rule proposed by the Association of American Railroads ("AAR") and the National Industrial Traffic League ("NITL") in Ex Parte 445 (described in our response to Supplemental Question 5 below), revenue adequacy would not be considered in such cases in the future.

Notwithstanding the results in Central States, a shipper in Central States' position would be more likely to meet the standards of section 11103 than to prevail under section 2 of the Sherman Act. This is because the ICC considers only intramodal competition under section 11103, and therefore a shipper need only show that switching is needed for competitive rail service. Under the Sherman Act, in contrast, the presence of intermodal or geographic competition would be relevant to determine whether the railroad had monopoly power over the shipper in any relevant markets. Geographic competition might be a particularly relevant issue for a grain shipper if the ultimate delivered price of grain is competitively determined. If so, this competition might prevent railroads from having monopoly power over grain shipments.

In addition, in order to obtain relief under section 11103, a shipper need not prove any unlawful monopolistic conduct, as it would have to do under the Sherman Act; it is enough to show that another carrier is needed for "competitive rail service." Thus, the only disadvantage to a shipper in proceeding under section 11103 rather than under section 2 is the possibility that, notwithstanding proof that the conditions described in section 11103 exist, the ICC can decline to exercise its discretion to grant relief to the shipper.

5. Mr. Rule, you mentioned in your testimony that another reason to forego the passage of S. 447 is that the Commission currently is in the process of promulgating regulations pertaining to competitive access issues in Ex Parte 445 (Sub. No. 1), Intramodal Rail Competition. As you are aware, one of the two proposals that the Commission has invited comments upon is an agreement between the National Industrial Transportation League and the Association of American Railroads. The substantive standards of that agreement are based upon the "competition policies" of 49 U.S.C. § 10101a, the Staggers Act Rail Transportation Policy. Do you think that the Commission should adopt language within the agreement as final regulations? Please explain your answer.

A. The Commission served a decision on October 31, 1985, that basically adopted the joint proposal of NITL and AAR with certain modifications, including features submitted by the Railroads Against Monopoly ("RAM") group. The Department does not object to the adoption of the proposed rule negotiated by NITL and AAR. The proposal is acceptable to large segments of the industry representing diverse interests and provides a framework for dealing with captive shipper issues in which competitive analysis is paramount.

The new rule sets forth how the ICC will handle protests of joint rate cancellations under 49 U.S.C. 10705, petitions for the establishment of through routes and joint rates under 49 U.S.C. 10705, and petitions for reciprocal switching under 49 U.S.C. 11103. Under the new rule, the Commission will exercise its authority to establish joint rates or compel switching when "necessary to remedy or prevent an act that is contrary to the competition policies of 49 U.S.C. 10101a or is otherwise anticompetitive." Thus--quite properly--competition is the standard to be applied in all such cases.

The new rule establishes similar standards for regulatory intervention to prohibit cancellation of existing joint rates, and the Department also has no objection to the proposal in this area. The ICC will only prohibit cancellations that it finds to be anticompetitive, and will only suspend a cancellation where the cancellation would "eliminate effective railroad competition for the affected traffic between the origin and destination." However, the ICC should be careful not to equate the elimination of an alternative routing with the elimination of competition. Properly applied, the standard is an appropriate prerequisite for suspension and will assure railroads reasonable flexibility in cancelling inefficient or non-remunerative joint rates.

Under the new rule, the ICC will not consider product competition in determining whether regulatory intervention is necessary to prevent or remedy anticompetitive conduct. In addition, if a railroad wishes to rely on geographic competition, it must prove the existence of such competition by clear and convincing evidence. While the Department might not have crafted precisely that rule to govern such cases, we believe that the ICC can lawfully decide to adopt such a rule.

The new rule also makes it clear that the ICC will not consider a carrier's overall revenue adequacy as an excuse for anticompetitive conduct.
The Department supports this approach, which is consistent with the Interstate Commerce Act. That Act requires the ICC to consider revenue adequacy when

determining the reasonableness of a rail rate for traffic over which a carrier has been found to be market dominant, see 49 U.S.C. 10701a(b)3, but the Act does not require the ICC to consider revenue adequacy when exercising its powers under 49 U.S.C. 10705 or 11103.

The Department considered the RAM proposal to be much less desirable than the NITL/AAR proposal in several respects, and supports the decision of the Commission not to adopt the RAM proposal to any large extent. The RAM rule would have made competition merely a factor to be considered, rather than the focus of the analysis. For example, the RAM proposal required suspension of joint rate cancellations based on mileage measurements, cost ratios, or where the "canceling railroad failed to provide a full explanation and justification for the cancellation. . . ." These tests might be met--and particular carrier action prohibited--even where the cancellation is not anticompetitive.

The Commission did adopt one of RAM's proposals in its suspension criteria, not as an absolute standard as RAM proposed, but as a rebuttable presumption. Under the RAM rule as adopted, the Commission will presume that a cancellation will eliminate effective competition if the cancelled route was no longer, and priced no higher, than any possible alternative rail route. The Commission's use of this test as a rebuttable presumption at the suspension stage is not unreasonable.

Inexplicably, the RAM rules would have exempted from their application railroads with less than two percent of the railroad industry gross freight revenue. There is no justification for such an exemption because the effects of anticompetitive behavior are the same regardless of whether the railroad involved is large or small, and we are pleased the Commission rejected this proposal.

STATEMENT OF SENATOR JEREMIAH DENTON

Mr. Chairman, I want to express my appreciation to you for holding hearings on competition in the railroad industry. I have heard from the utility and coal industries in Alabama about this issue. They have expressed a great concern about the effects of transportation costs on their business.

The legislation that is the subject of this hearing, S. 447, focuses on the problems affecting the "captive shipper." Since enactment of the Staggers Act of 1980, many shippers have been satisfied with the transportation service provided by the railroad industry. Deregulation has given the industry the flexibility to become more efficient and regain some of the economic prosperity that it once enjoyed.

I have been told, however, that, in many cases, the captive shipper is required to pay high rail rates because of the lack of alternative means of transportation. Higher rail rates to the coal industry can result in higher utility rates to the consumer and reduced exports on American coal.

Representatives of the Association of American Railroads will testify that rail rates for coal have not risen dramatically since 1980. Captive shipper interests tell a different story. I hope that our hearings will provide a clearer picture of the current situation.

I do not want to see the railroad industry strangled with excessive regulation. I also do not want the captive shippers to be unfairly charged for transporting their product. I look forward to reviewing the hearing record on this issue.

Thank you, Mr. Chairman.

Senator McCONNELL. I have a couple of questions here that Senator Thurmond wanted to propound to you, Mr. Rule.

Could you describe the essential elements of a monopolization case under current antitrust law?

Mr. RULE. The essential elements currently are a showing of monopoly power or a reasonable probability of achieving monopoly power, and some act, what would be known as a bad act, essentially an act of excluding competition or trying to monopolize.

The fact that a particular activity is deemed not to be a competitive price charged by a single entity is not deemed to be monopolization in and of itself. And generally the anti-trust laws do not preclude the charging of price allowed by a particular market power possessed by an individual, but rather requires the showing that there is some sort of monopoly power combined with an act that constitutes monopolization or attempt to monopolize.

Senator McCONNELL. Does the Department of Justice believe that current antitrust law provides adequate remedies for shippers that may be subjected to monopolistic practices by railroads?

Mr. RULE. I would slightly broaden what we think provides adequate remedies. It is true that under section 16 of the Clayton Act, which provides for injunctive remedies, injunctive relief is not available in the case of rail carriers.

We believe, however, that the provisions of the Interstate Commerce Act, in combination with other provisions of the Sherman Act that prevent predatory pricing and that sort of thing, are adequate at this time so far as we know to prevent any anticompetitive abuses. Although, as I have stated, we look forward to the record developed by this committee and also actions by the ICC in confirming our belief that there are adequate remedies.

Senator McCONNELL. Thank you, Mr. Rule.

Senator Denton.

Senator DENTON. Mr. Chairman, I have a statement that I will be submitting for the record. The summary of it is that I do not want to see the railroad industry strangled with excessive regulation. I also do not want to see captive shippers unfairly charged for transporting their products with an ultimate higher cost to the consumers of those products. I will carefully review the record of this hearing.

I have heard from many shippers in my State about this issue. I am interested in it and I am pleased that you are holding hearings on the issue of competition in the railroad industry. Thank you, Mr. Chairman.

Senator McConnell. Thank you, Senator Denton.

If there are no other questions of Mr. Rule, we will go to—thank you very much.

Mr. Rule. Thank you, sir.

Senator McConnell. We will go to a panel of Paul Donovan and Ira McKeever. Mr. Donovan is from LaRoe, Winn and Moerman here in Washington. Mr. McKeever is the president of Western Coal Development Division of W.R. Grace and Co., Denver.

As I guess you heard the chairman say, you can limit your remarks to 5 minutes each, and we will take your full statement for the record.

STATEMENTS OF PANEL INCLUDING HON. PAUL M. DONOVAN, LaROE, WINN & MOERMAN, WASHINGTON, DC; AND IRA E. McKEEVER, JR., PRESIDENT, WESTERN COAL DEVELOPMENT, W.R. GRACE & CO., DENVER, CO, ACCOMPANIED BY JOHN N. THURMAN, GROUP VICE PRESIDENT, W.R. GRACE & CO. WASHINGTON, DC

Mr. Donovan. Thank you, Mr. Chairman.

My name is Paul M. Donovan. I have submitted a statement in advance of the hearing and I would request that it be entered into the record.

Senator McConnell. Without objection.

Mr. Donovan. Thank you.

Rather than simply summarizing that statement at this point, I would like to comment, if I might, on some of the points that Mr. Rule just made. I think that might be more useful for the committee.

I want to begin by saying that the overall thrust of S. 447 is, in my judgment, a very useful one. At the moment, there is a clear hiatus between the application of the Interstate Commerce Act and the application of the antitrust laws. A void, if you will, caused by deregulation of an industry which for a hundred years has been pervasively regulated. Right now there is simply a hole in the applicable laws.

Having said that, I must suggest that there are certain provisions of S. 447 which are not totally acceptable from my view. I think Mr. Rule may have hit upon a couple of those points, one particularly. That is the provision that would create a new section 9(a)(3) of the Sherman Act which would provide the district court with regulatory power over a railroad's rates even in those circumstances where the railroad has done nothing to either create the monopoly or maintain it. If it in fact had committed no bad act, as Mr. Rule has stated. I have to agree with that.

It seems to me that the district court regulating rates in those circumstances is simply inappropriate. The Interstate Commerce

Commission is charged with the obligation of regulating those rates, and if they do not do it properly, that, it seems to me, is not the function of the antitrust laws but of some oversight on the part of Congress.

Having stated that, however, I would like to say that I cannot fully agree with Mr. Rule's statement that the scope of the captive shipper problem is exaggerated, not defined or overly broad. The captive shipper first must be defined. A shipper is not captive simply because he only has access to one railroad. There may be significant market forces that even though he only has access to one railroad serve to keep his rates down to a reasonable competitive level. Mr. Rule suggested motor carrier competition, geographic competition, product competition. To be sure, those things do operate in the free market.

My definition of a captive shipper is a shipper who has none of those alternatives available to him. And so his rates have gravitated up to the monopoly level. That is my definition of a captive shipper.

Those instances do exist. They are significant in the railroad industry, and it would serve no useful purpose to sit here and give examples of them. But there are many, many situations where railroads have taken deliberate actions to maintain that monopoly power. Thereby, raising rates to the monopoly level.

Is the Staggers Act protection adequate to keep rates at a reasonable level? I suggest to you no for two reasons. No. 1, I do not think it is the sole charge of the Interstate Commerce Commission to regulate rates without regard to the profitability of the railroad. I think one of their major charges is to keep the railroad profitable. That is not a competitive goal; that is a social goal.

Second, it seems to me that we have proved beyond question that competition rather than regulation is the far more effective regulator of market prices. I think that S. 447's thrust would permit competition into the marketplace to the maximum extent possible, thereby exercising a moderating effect upon rates.

Mr. Rule stated that in those circumstances where there already is competition that S. 447 would provide some overlapping unnecessary power. Well, I submit that S. 447 absent the 9(a)(3) provision, the regulation provision, would not do that. The simple reason is that if there is already a force that is keeping rates down at a competitive level, the prod to enter that market is no longer there. No shipper in going to invest in a railroad or start building railroad tracks or operating over railroad tracks, or doing anything of that kind if his rates are already at the competitive level. There is simply no prod to do it.

As for the rate distortions that Mr. Rule talked about, I think again that is a function of the 9(a)(3) provision. Absent 9(a)(3), I see nothing in this bill that would artificially create rate distortions.

As to whether the provisions of S. 447 are redundant with the Interstate Commerce Act reciprocal switching provisions, no, I think no. The Interstate Commerce Commission again, as I said, is charged not only with promoting competition but from its view, I suspect, more importantly, it is charged with an obligation to make sure that the railroads are revenue adequate. I can cite to you, Mr. Chairman, where the Commission, faced with a reciprocal switching request where one railroad came and said I want access to this location so I can provide competitive rail service, and the other carrier declines, the Interstate Commerce Commission said that the declining carrier was revenue inadequate and should not be forced to give up the monopoly.

Mr. Rule, in his prepared testimony, suggests that perhaps the essential facilities doctrine that this bill really addresses is not a good doctrine because it prevents an investor from earning a return on his investment. I do not think that the Congress or that the courts have taken a position that AT&T, for example, should be able to charge whatever it wants to on its long distance phone rates because it made the investment. I think the social and economic goals of allowing competing telephone companies, such as MCI, into the market have stood up in good order.

In summary, I would just say that I agree fully with Mr. Rule when he suggests that the Sherman Act should not be a regulatory statute. It should be a statute which permits free market forces to operate. And S. 447, with two or three relatively minor modifications, I think will achieve that goal of allowing market forces to operate and getting the Federal Government out of the regulatory business to the maximum extent possible.

Thank you, Mr. Chairman. If you have any questions, I would be happy to try and answer them.

Senator McConnell. Thank you.

Why do we not go to the next witness.

STATEMENT OF IRA E. McKEEVER, JR.

Mr. McKeever. Thank you, Mr. Chairman. I have with me today John Thurman, our vice president here in Washington. And I want to thank you for allowing me to present this overview of my written statement which I would like to have submitted in its entirety in the record.

Senator McConnell. Without objection, that will be done.

Mr. McKeever. I would like to also say that I am representing producers of bulk commodities that fully support S. 447.

I would also like to thank the ICC for their inactivity in protecting the captive shippers, because that has revealed what is broken in the deregulation of the railroads. Likewise, thanks should be given to the railroad managements for setting monopoly rates for sole access facilities. The ICC's inaction and the railroads' actions have set the stage for fixing the applicability of the Sherman-Clayton antitrust laws. Without this background, I doubt that we would have found the drive and desire to take on the deregulated monopoly that controls the financial destiny of many captive coal mines.

This committee heard 3 weeks ago during the Conrail hearings of the adverse impacts of eliminating rail competition for the delivery of coal in the Northeast.

Where monopoly service already exists for coal, grain and other bulk shipments, monopoly pricing has already occurred. In other words, the great runup in coal transportation prices predicted by your witnesses at the Conrail hearing as a potential result of further mergers and monopolization are already being borne by the consumers of coal from sole access rail transport areas.

In the West, on a State-by-State basis, 70 to 100 percent of the coal shipped by common carrier is captive to monopoly railroads.

The mere introduction of rail competition by Chicago and Northwestern into the Burlington Northern's sacrosanct Powder River Basin area served has resulted in coal rate reductions of 30 percent. Profit potential even at these reduced levels is still so great as to prompt the Chicago and Northwestern to propose construction of a $25 million, 10-mile duplicate track to reach additional mines. S. 447 would provide competitive access so this folly would not have to be built and its cost borne by the consumer.

Monopoly rail pricing of coal movements is of concern to utilities.

For instance, the Colorado-Ute Electric Association supports the application of the antitrust laws to monopoly railroad rates in order to assure more competitive pricing of coal movements, even though the utility has just negotiated downward a particularly onerous rate imposed by the Denver and Rio Grande Western.

Coal mines and utilities are not the only ones affected by monopoly pricing.

Freight rates charged Montana wheat growers are considerably higher than those in neighboring States.

The Burlington Northern's earnings per car mile on grain from points in Montana to the Pacific north coast are $4.22. That is 62 percent higher than earnings for grain movements from Kansas, Nebraska, and Colorado to the Pacific north coast.

The difference: competition for rail service. It does not exist for the Montana growers.

Let us look at phosphate in Florida. Most of the phosphate companies in Florida are captive rail shippers.

The Florida Phosphate Council Board of Directors strongly supports S. 447 and urges its passage, stating, "The proposal does not reregulate, it is the logical conclusion to the deregulation process by placing railroads under antitrust laws in enhancing competition in the marketplace."

Monopoly rail pricing is particularly harmful to exports. Given our great imbalance of trade, it should be particularly galling to know that monopoly rail rates are a key determinant in the decline in coal exports. This was pointed out to the committee by Morgan Massey 3 weeks ago in the Conrail hearings.

Twenty months ago, this was pointed out to the Southern Governors' Association in a teleconference with European energy and coal managers. The Europeans stressed that excessive monopoly rail rates are a key cause of reduced coal exports from the United States. This was reinforced again in February of this year at the Third World Coal Conference held by the Mississippi Valley Coal Exporters Council in New Orleans.

In closing, the essence of S. 447 is to set rail freight rates through competition and not regulation. Competition, the self-regulator of our free market economy, compels companies to minimize cost, produce quality goods and services, forces innovation, and holds the lid on prices.

For the railroads, that means a more efficient industry. And for the consumer, it assures the least cost for electricity and other products, and that is why we need S. 447.

Now, finally, Mr. Rule indicated that S. 447 is regulatory in nature. I strongly disagree unless the Sherman Act is considered regulation. If so, I am unaware of that label.

Thank you.

Senator McCONNELL. Thank you.

Senator Thurmond has got a two-part question for Mr. Donovan. Would you please describe the essential elements of a monopolization case under current antitrust law and under current laws enforced by the ICC?

And then the second companion question is: Could you please explain whether you think that it is difficult to prove such a case and, if so, why?

Mr. DONOVAN. Mr. Chairman, I would agree with the general definition of the section 2 violation that Mr. Rule gave. You have to show that the monopoly power or the substantial likelihood of acquiring that power exists and that the monopolist or potential monopolist has done or is doing something to acquire or maintain that power. The bad act, so to speak.

Under the Interstate Commerce Act, I do not believe that the concept of monopoly power is recognized. It is not there.

Under the second part of the question: Is it difficult for a shipper to demonstrate? The answer to that is fairly complex in that, one, even if a shipper does succeed in demonstrating monopoly power, his potential remedies do not really exist under the Sherman Act. Certainly, as Mr. Rule indicated, there is no injunctive power simply because section 16 of the Clayton Act precludes railroads from being subjected to that injunctive relief.

Second, under a case decided by the Supreme Court in the twenties, the *Keogh* case, which I believe Mr. Palmer will discuss at some length, shippers simply do not have a right to treble damages in these circumstances. It is suggested by the Supreme Court that the ICC determines what a reasonable rate is and that the measure of damages against the railroad are the differences between a reasonable rate and a monopoly rate. Well, since the reasonable rate is already prescribed, there can be no measure of damages. Your damage is zero. So, even trebled, they are still zero.

Now, in the recent literature, the *Keogh* case has been criticized extensively. But the second circuit in a very recent decision has said it is still the law, and if it is to be changed, it can only be changed by the Supreme Court. I do not think a shipper is going to be anxious to buy a Supreme Court case before it challenges a railroad.

Senator McCONNELL. Mr. Feidler, do you have some questions on behalf of Senator DeConcini?

Mr. FEIDLER. Yes. Thank you, Mr. Chairman. I have some questions for Mr. Donovan.

Do you agree with the basic concept of this bill that the antitrust laws as they regulate competition should be fully applicable to the rail industry?

Mr. DONOVAN. Unequivocably, yes.

Mr. FEIDLER. Do you agree that the rail industry is partially exempt now from the antitrust laws?

Mr. DONOVAN. I think there can be no question of that. Yes; it is partially exempt.

Mr. **Feidler**. Is it realistic to expect that a shipper could win a section 2 antitrust case now against a railroad?

Mr. **Donovan**. No. As I indicated in my response to Senator Thurmond's question, it may be possible, but realistically, in the real world, it is extremely unlikely.

Mr. **Feidler**. Would you view S. 447 as a logical extension of the deregulation process begun in the mid-seventies that culminated with the Staggers Act? Will this bill fill a void in the law affecting the rail industry?

Mr. **Donovan**. I think that a piece of legislation very much like S. 447 would accomplish that result; yes.

Mr. **Feidler**. Do you think that the provisions of the Staggers Act affecting captive shippers have worked?

Mr. **Donovan**. I think to answer that question I have to go back to my definition of a captive shipper. I think to the extent that the captive shipper may benefit from other market forces, the answer to the question is probably yes; it has resulted in a situation where a shipper can use competition more freely to negotiate with a railroad. Equalized railroad rates are no longer the norm.

However, as to a truly captive shipper, one without competitive alternatives, the answer is no. The Staggers Act has not protected them from price gouging.

Mr. **Feidler**. A number of Senators have sponsored a somewhat similar bill to S. 447, entitled S. 477, which would supplement to a degree the Staggers Act. Senator DeConcini has also cosponsored that bill, and Senator Andrews, the lead sponsor of that bill, has cosponsored this bill.

Which bill do you prefer and which do you feel would be more effective in spurring competition?

Mr. **Donovan**. I think that S. 447, the bill here under discussion, is by far preferable, so much so that I would say S. 447 is objectionable I do not think it is a useful piece of legislation. I think it reregulates rather than allowing competition to set the market, which I think answers the rest of your question. S. 447 is clearly the most competition-oriented bill.

Mr. **Feidler**. Section 3 of the bill before us adds a new section 9(a) to the Sherman Act. Section 9(e) specifically enumerates who can utilize it. It lists a series of bulk commodity shippers.

Do you feel the bill should specifically enumerate the bulk commodity shippers that can use this antitrust remedy, or should it be open to all shippers?

Mr. **Donovan**. I think it should not only be open to all shippers, I think it should be open to all persons who may be adversely affected. It does not take much thought in the current scheme of things to recognize that the Santa Fe and the Southern Pacific may well merge before the ICC. I think that is of particular concern to Senator DeConcini in Arizona where both railroads operate.

The same thing is true with respect to the Norfolk Southern and Conrail. Those situations could result in markets where entire municipalities may be subject to railroad market power. I see no reason to foreclose a municipality, for example, from trying to bring an action to promote additional competition.

It seems to me that to the extent that a market is monopolized, that market ought to be the subject of this bill. Hence, I would remove the bulk shipper definitions entirely and simply allow it to apply as the market would indicate.

Mr. **Feidler**. Do you feel that would place the railroads in an untenable position to have to deal with all persons?

Mr. **Donovan**. No, I do not think so at all.

Mr. **Feidler**. What do you feel the appropriate test should be to determine if an antitrust violation has occurred? For example, the bill sets a monopolization standard. Would a "substantially lessening of competition" standard as found in section 7 of the Clayton Act be a good substitute or good supplement to the monopolization standard?

Mr. **Donovan**. A good supplement, yes. I believe it would for this reason: frequently railroads, even when they face competition from other railroads, face it in a duopoly situation. You have twc carriers after the same traffic. Those carriers recognizing they have a certain market share in many circumstances are very unlikely to actually compete. If they do, they can expect their other railroad to respond accordingly in a price circumstance, thereby simply depressing the price without having any increase in market share. Duopolies are not very competitive.

However, in that circumstance, where neither railroad possesses monopoly power, if either of those railroads were to prevent a shipper, for example, from entering the market in order to provide a competitive rate, there would not be a monopolization but there would be a substantial reduction of competition. So I think that the test should be monopolized, attempt to monopolize, or substantially reduce competition.

Mr. **Feidler**. Mr. Rule, in his prepared statement, commented on the role of the Federal courts.

Could you comment on how the Federal courts might handle both quantitatively and qualitatively litigation that this act might spawn?

Mr. **Donovan**. Well, I have to agree with Mr. Rule if 9(a)(3) remains in the bill. If it is in fact the situation where the Federal district court will be, and presumptively a Federal district court jury or judge would be establishing what a reasonable rate is within the meaning of, I guess, public utility regulation generally. I think this would be an extremely damaging provision. You would have district courts in one place coming to one conclusion, and a district court in another place coming to another conclusion, and frustrated shippers filing perhaps unnecessary litigation.

On the other hand, given the treble damage and injunctive relief provisions of the bill, if a railroad recognizes that it is subject to treble damages for monopolization practices or for price gouging when it is in fact an active monopolist, or someone who is substantially reducing competition, the disincentive for them to run that risk is there. Hence while the antitrust laws, it can be said, produce a good deal of litigation, they also prevent a great deal of competitive harm by people who are afraid to contravene them. They simply do not commit the bad act.

The Interstate Commerce remedy simply does not provide that. You can litigate for 5 years at the Interstate Commerce Commission, and even if you win on appeal, you get no damages. So the incentive on the part of the railroad is to continue its noncompetitive practices knowing that there is no sanction at the end of the road. This bill would change that.

Mr. FEIDLER. Do you believe the bill should include some form of essential facility standard to judge reasonableness?

Mr. DONOVAN. Yes, I do. Well, in the sense that—I am not sure the bill needs to in hic verba say essential facilities. I think the way the bill is presently structured, if 9(a)(3) is removed, the essential facilities doctrine developed by the Federal courts in monopolization cases would be the logical test that the courts would apply. I see no reason for the courts to vary or depart from that course.

Mr. FEIDLER. Recent developments in the long distance telephone market as a result of the MCI case have precluded AT&T from extending its local monopoly into the long-distance market.

Do you feel this was in the public interest?

Mr. DONOVAN. Oh, absolutely.

Mr. FEIDLER. Does the same principle apply to the railroad industry?

Mr. DONOVAN. Without question. There is one other scenario that I think we may not have touched upon that we should. Mr. Rule suggested the reciprocal switching situation where locally two carriers exist but only one actually serves the locality thereby permitting a monopolization by not allowing the second carrier in.

The remedy, he suggests, is reciprocal switching where the dominant carrier is forced to turn the cargo over to the second carrier for long-haul competition.

There is another form of monopolization that occurs, and I think probably Florida with phosphate rock is the best example of that. In Florida, most of the phosphate rock, virtually all of it, sits on the lines of the CSX in Bone Valley. The CSX journeys northward to Jacksonville. At Jacksonville there are two carriers. Now, that is quite a haul. It is not a reciprocal switch. It is a long distance haul. At Jacksonville, the CSX can either continue to move it or it can be turned over the Norfolk Southern.

Now, obviously if it can be turned over to the Norfolk Southern, the transportation between Jacksonville and the ultimate destination is going to be competitive. CSX has moved in and said we will not allow you to transfer that freight to the Norfolk Southern. It will stay on our lines until we choose to give it up. And the Interstate Commerce Commission has said that is fine, that is wonderful.

Now, that, I think, is a clear case of a reduction in competition, a substantial reduction in competition, maybe even a monopolization. But the Interstate Commerce Commission has blessed it. And now it is unreachable under the antitrust laws and under the Interstate Commerce Act.

Mr. FEIDLER. When the airlines were deregulated, they came completely within the scope for the antitrust laws, is that correct?

Mr. DONOVAN. Largely, yes, that is true.

Mr. FEIDLER. Mr. McKeever and Mr. Donovan, are you generally familiar with the hearings this committee held 3 weeks ago on the Conrail and Norfolk Southern sale?

Could you comment how this bill might impact some of the antitrust questions that were raised in those hearings?

Mr. McKeever. I think that this bill would definitely reduce the impact of the merger if it went through by allowing the opportunity for competition to exist on the merged track. I think this fixes that merger.

Mr. Feidler. Thank you, Mr. Chairman.

Senator McConnell. Section 2(c) states that S. 447 will prohibit carriers from accessing charges on terms less favorable than those that would be assessed or required in a truly competitive environment.

How will the courts determine what those charges will be?

Mr. Donovan. Mr. Chairman, I think that that is always a problem in any monopolization situation.

The answer to the question has been varied from court to court depending upon the circumstances. It is not possible, it seems to me, to have an ironclad rule. For example, in the *Otter Tail* case, which is a leading case in monopolization, the large power company maintained its monopoly in a local market by refusing to sell to a local power company at wholesale rates. In that situation, permitting thereby the local power company to sell at retail rates and earn a fair profit, and provide competition to the dominant power company. In that situation, the court held failure to sell at wholesale rates was unlawful.

In other circumstances, the MCI case, for example, the court had to examine what a fair access charge for local access to the local phone system would be. It was not an easy test.

In most of these cases, quite frankly, Mr. Chairman, the court simply says you two people work it out and if you cannot, I will. And that is a sufficient prod to make the two people sit down and work it out.

Senator McConnell. OK. Thank you very much. I appreciate your comment. I thank the witnesses.

[Prepared statements follow:]

TESTIMONY OF
PAUL M. DONOVAN

Mr. Chairman and members of the Committee, I want to express my gratitude for being invited to testify at the behest of the Committee in connection with Senate Bill S.447.

Let me begin my saying that I strongly support the concept embodied in this bill. I agree completely that the antitrust laws and their full application to the railroad industry is the next logical step in the steady, bipartisan process of deregulating this Nation's railroads.

I personally have been involved in transportation and the practice of transporation and antitrust law for nearly twenty years. During this time, I have witnessed an important fundamental change in the railroad industry, especially with regard to its status as classic example of a regulated public utility.

In the 1960's and even into early 1970's the railroad industry was pervasively regulated by the Interstate Commerce Commission. Virtually every aspect of railroad business was governed in one form or another by the Commission, including the issuance of securities, the incurring of financial obligations, and the pricing of services. Frequently, the simplest form of railroad rate activity, be it an increase or a decrease, was subject to bitter ICC struggles by shippers or competing carriers, and a railroad's ability to price in a sensible and flexible manner was impeded, if not completely frustrated. Members of this Committee, of course, are well aware of the fruits this regulatory burden--large scale inefficiency and even financial collapse. A statutory scheme intended to protect the shipping public in the long run was operating to its detriment.

Beginning with the 4R Act in 1976, the Congress set upon a new course of "regulating" the railroad industry. The design was to permit market forces, to the maximum extent possible, to determine railroad rates and activities. However, for a variety of reasons the 4R Act was not completely successful in accomplishing these laudetory goals. Accordingly, in 1980 the Congress passed the Staggers Rail Act and took another significant step toward railroad deregulation. I needn't review here the various amendments to the Interstate Commerce Act made either by the 4R or Staggers Acts. Suffice it to say that, today, railroads largely have been freed to operate in the same manner as unregulated business in the general economy.

In my opinion, this unquestionably is a positive development, and the experience of most shippers over the last several years bears this out. Generally, rail rates have risen at a level in keeping with inflation but not beyond that. Some rates actually have fallen, while railroad efficiency unquestionably has improved.

The question becomes, why is the legislation you are examining today necessary? Why cannot individual problems arising from individual railroad abuse of market power be handled under the antitrust laws, as in the case of unregulated businesses generally?

The answer is that, seemingly contrary to what I have already said, the 4R and Staggers Rail Acts did not undertake total railroad deregulation. Much unnecessary regulation was removed, but the actual regulatory structure, under the tutelage of the ICC, remains. This necessarily restricts the application of the anitrust laws.

During the period when railroads were pervasively regulated, most of the Nation's antitrust laws were evolving. Both legislatively and judicially it was apparent that, given the existence of pervasive railroad regulation, application of the antitrust laws and their principles to this industry largely was unnecessary, even counter-productive. However, since the industry is now only partially regulated, that rationale, which underlies the various relevant legislative and judicial exemptions, no longer is valid. Nevertheless, the exemptions remain.

It seem to me, therefore, that it is clearly time for Congress to review these exemptions. Specifically, Congress should determine whether, in today's deregulatory environment, the railroad industry should be made fully subject to the current antitrust laws. Also, Congress should determine whether, in view of special circumstances surrounding the railroad industry, certain other steps need to be taken to protect and promote transportation competition.

Beginning with S.2417 in the last session and continuing with S.447 today, Congress seems prepared to closely examine the antitrust laws and their underlying principles with respect to their actual or potential application to the railroad industry. With this effort I wholly agree. To be candid, however, I must confess that I see certain problems with the current version S.447, although I don't believe that those problems detract from the overall thrust of the legislation.

In my opinion, in some areas S.447 does not go far enough in making antitrust law concepts applicable to railroads; in other areas I believe that S.447 goes too far in attempting essentially to substitute the federal courts' regulatory jurisdiction for the jurisdiction of the Interstate Commerce Commission. All in all, however, I believe that the thrust of the legislation is positive and that S.447, or a bill very much like it, should be enacted by the Congress. Indeed such legislation is becoming absolutely essential.

Mr. Chairman, members of the Committee, once again I want to thank you for this opportunity to present testimony on this very important issue. If you have any questions, I would be more than happy to try and answer them. Thank you.

Paul M. Donovan

LaRoe, Winn & Moerman
1120 G Street, N.W.
Washington, D.C. 20005
(202) 628-2788

Testimony Before the

COMMITTEE ON THE JUDICIARY

U.S. Senate

By
Ira E. McKeever, Jr.
President
Western Coal Development
W. R. Grace & Co.

Mr. Chairman, it is a pleasure to provide support for S. 447, the Railroad Antimonopoly Act of 1985.

The nation's coal industry is heavily dependent on railroads to move its product to market. Current coal production is at a rate of 890 million tons per year. Of this, approximately 63%, or 561 million tons, is moved by rail to its destination, and a substantial portion of this is captive to individual railroads for all or an essential part of its transport.

By captive, I mean that alternative transportation options, be it by a competing railroad, truck, barge, pipeline or conveyor, are either not available or within the realm of economic or social practicality.

The Captive Coal Situation in the West

Substantial production and reserves, in the Western United States, are captive to a single railroad. For instance, I estimate that 97% of coal production, moved by common carrier in Colorado, is captive to one railroad. Similar estimates for other western states are:

Utah	80%
Wyoming*	70%
New Mexico	100%
Montana	100%

* Note: Competitive rail service is due entirely to joint use of facilities - see page 8 of this statement.

As an example, let me address our specific problem in northwestern Colorado. Grace is a partner with The Hanna Mining Co. of Cleveland, Ohio, in the Colowyo mine and the Hayden Gulch mine.

The Colowyo coal mine is the largest coal mine in Colorado, producing over three million tons of coal per year and employing over 400 people. The total investment in the mine exceeds $100 million. The Hayden Gulch mine is producing about half a million tons per year. In addition to these two operating mines, we own federal, state and private coal leases at three other sites in northwest Colorado (Hayden Gulch West, Little Bear Creek and Chokecherry). The combined capacity of these five properties, if fully developed, would be in excess of 8 million tons per year, more than double our current production capacity level of 3.5 million tons.

The reason we have not further developed these properties is that we have been unable to obtain any long-term contracts since 1980. In fact, we have recently found it necessary to renegotiate one of our existing contracts (with Celanese Chemical Corporation), which will result in closing down the Hayden Gulch mine at the end of 1986, putting 60 people out of work. We have also been advised by another of our long-term buyers, Central Power & Light Co. of Corpus Christi, Texas, that they do not intend to exercise their option to purchase additional coal, beginning in 1990, and will phase out their purchases of Colowyo coal by the end of 1994.

The principal reason we have not been able to negotiate any new long-term contract since 1980, and the reason we are losing existing long-term contracts with Celanese and Central Power & Light is the rapid increase in freight rates experienced by our customers as a result of the monopoly position of the Denver & Rio Grande Western Railroad. All coal produced by our two operating mines or to be produced from the other three properties, is captive to the D&RGW Railroad.

Inordinately high freight rates also prevent us from supplying additional spot market coal, on an annual basis, to Central Power and Light. Last year, coal from the Colowyo mine delivered to CP&L was ranked 14th on competitive bid list even though we were informed on the basis of the f.o.b. price of the coal and quality, our bid was ranked first. The attached recent article from the American Mining Congress Journal, addresses this situation more fully.

Let's look further at the Central Power & Light case. In 1977, when the coal contract was entered into, the D&RGW rate quoted to Central Power & Light was $13.00/ton. When shipments started at the end of 1979, the actual rate was $20.85/ton, a 60% increase in two years. The last I've heard the freight rate is $29.93/ton, an increase of 130% over the quoted amount at the time of contract. Even before the Staggers Act, the D&RGW's monopoly position allowed the railroad to take unfair advantage of its captive shipments. This situation has been exacerbated since the deregulation of the railroads.

Similarly, our coal shipments to the Celanese plant in Pampa, Texas, cost $11.14/ton in late 1980. It is now $16.51/ton, an increase of 48% in slightly more than four years.

Last year, within Colorado, shipments of coal from Colowyo to the Colorado-UTE Electric Association to a utility about 23 miles distant were quoted a cost of 11 cents/ton mile (vs. independent estimate of 4.5 cents/ton mile) over track that is for the most part owned and maintained by Colowyo. We estimated this rate to be approximately 400% over the direct costs to D&RGW in the provision of locomotives and crew and would have yielded well over 100% return annually to the D&RGW on their investment allocated to the operation. After our testimony before you last September, the D&RGW allowed negotiations with the Colorado-UTE Electric Association to be concluded and a rail haul contract resulted. Under the provisions of the Staggers Act, the terms of this contract cannot be made public.

However, I want to draw your attention to the enclosed statement from the Jerry Kempf, Colorado-UTE Electric Association, which supports the full application of the antitrust laws to the railroads, e.g., the enactment of S. 447. In his words:

> "Antitrust provisions that currently exist in today's law in the Sherman and Clayton Acts would prevail and competition in railroad pricing would be resolved."

Comparison: Colorado Coal and Railroad Prices

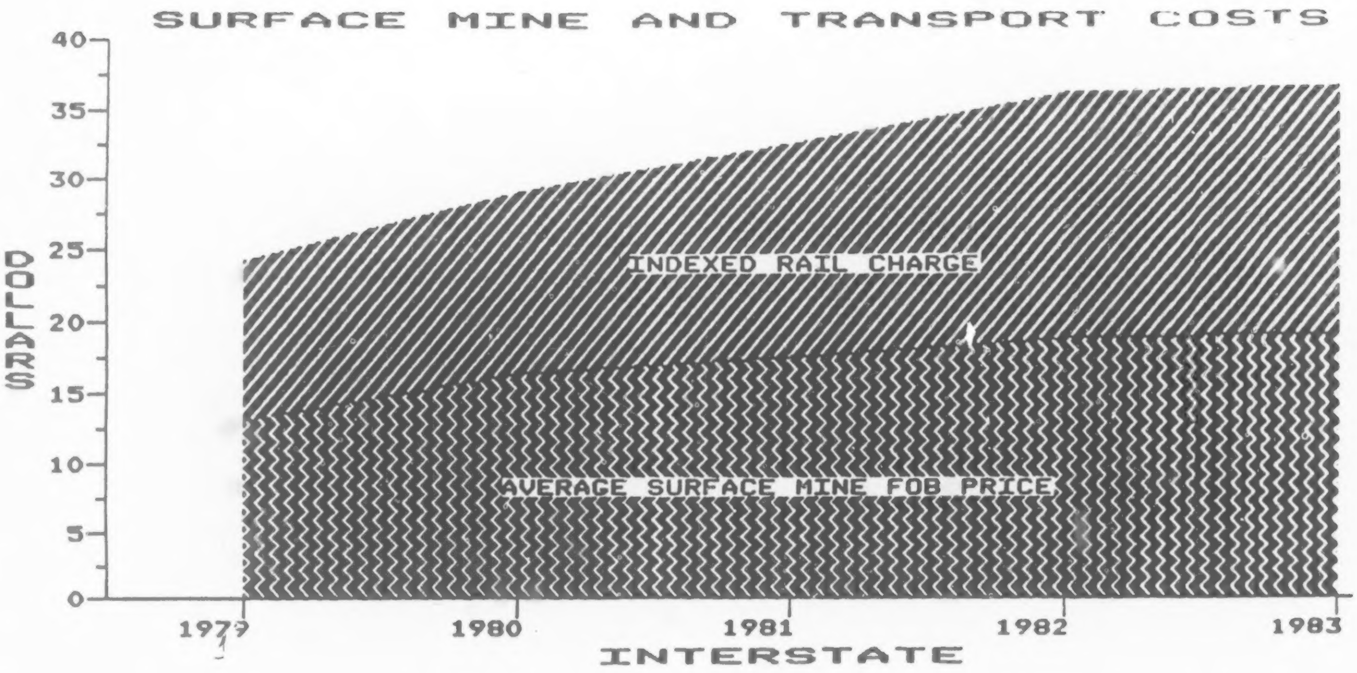
Since 1980, the price of surface-mined coal in Colorado has increased at a rate of 5% a year. Rail rates to haul this coal on an interstate basis have risen at a rate of 12.5% per year during this period. I should note that this rate of increase will double the cost of rail shipments in about six years. These two rates of increase are shown on the following graph, "Surface Mine and Transport Costs" [Figure 1]. Rail rates on the intrastate shipments of coal have risen at a faster rate, as shown on the second graph, "Rail Rate Increases" [Figure 2]. This second graph clearly shows the significant jump in rail rates, after the effective date of the Staggers Act. In the previous year, the interstate freight rate for Colorado coal was starting to drop.

The Captive Coal Situation in the East: Impact on Exports

Similar captive coal situations exist in the East. Portions of Eastern Kentucky, West Virginia, Tennessee and other Appalachian states are served by individual railroads only. While trucking offers alternative transportation for short distances, and many of this region's waterways are navigable, a significant portion of coal produced remains captive to individual railroads.

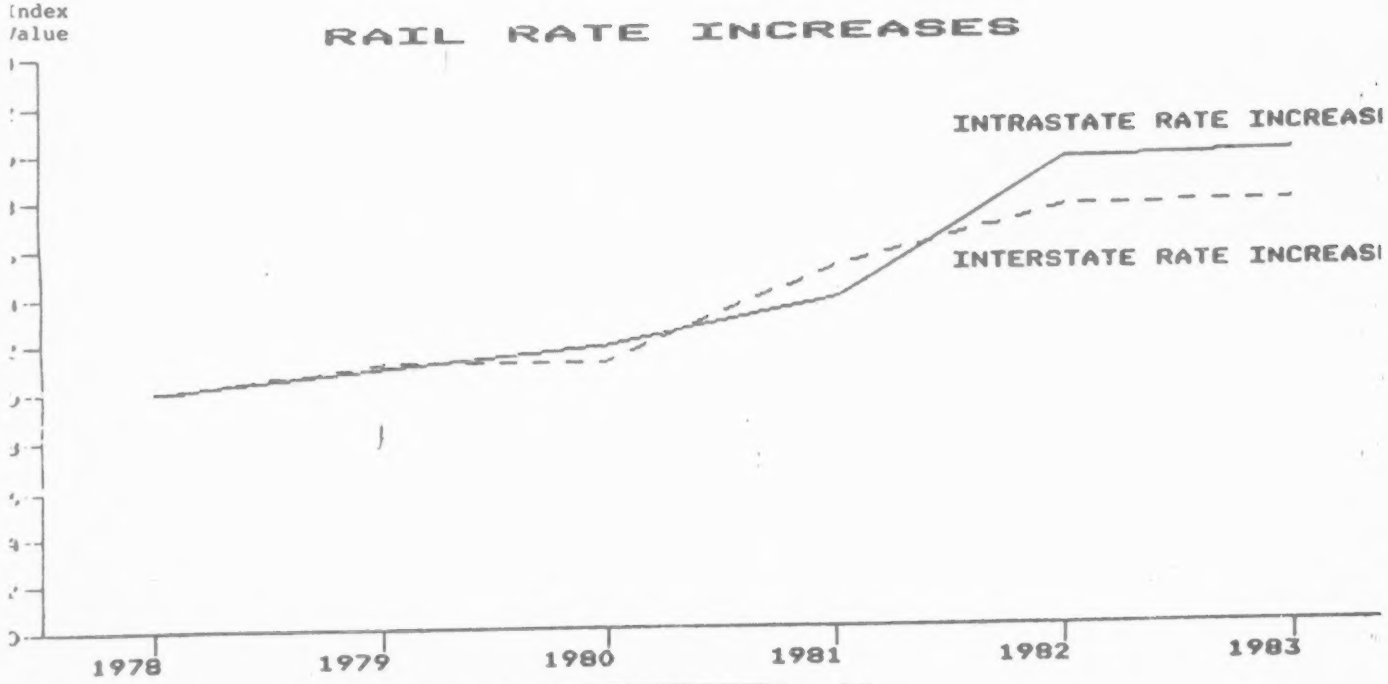
The impact of this captive situation is dramatically represented by the case of rail rates for coal exports - a distance too great for trucking and along East-West corridors from the coal fields to Eastern ports (Charleston, Hampton Roads, Baltimore, and Philadelphia), where waterways are not a factor. Since 1980, these unrestricted and monopolistic freight rates have increasingly destroyed the competitive position of the United States coal in the world market.

FIGURE 1



Based on: Analysis of the Colorado Coal Industry,
Peter Rushworth, Colorado Geological Survey
Department of Natural Resources, 1984

FIGURE 2



Derived from: "Table 4-9 and 4-10, Inter- and Intra-State Rate Increases on Coal." in Analysis of Colorado Coal Industry, Peter Rushworth, Colorado Geological Survey, Department of Natural Resources, 1984.

Export coal rates skyrocketed from $9.00 per ton to nearly $17.00 per ton. This, for instance, impacted A. T. Massey Coal Company's export tonnage, which dropped from 9.1 million in 1980 to only 3.6 million tons last year, even though the A. T. Massey Coal Company invested substantially to provide needed coal terminal facilities at Charleston, South Carolina.

I understand one of the chief reasons A. T. Massey located a new coal export facility in Charleston was to avoid the captive rail situation with which they were faced at their existing facility in Hampton Roads.

Railrates to the A. T. Massey Charleston facility for a short time appeared competitive. But now, rates have settled out at a level to match railrates to Hampton Roads. Railrates are set on the basis of how much the carrier can extract, given its monopoly (or duopoly) position; not on the basis of actual costs plus a fair profit.

In other words, for A. T. Massey, I understand there is no discernable advantage to moving coal through Charleston compared to other options. The rate making of the two railroads serving the Charleston facility provides no greater competition than that of the single carrier serving the Virginia Ports.

This is not an isolated example.

Escalating and monopolistic rail rates were cited to the Southern Governors as a key reason for the significant decline in U.S. coal exports by European energy officials during an international teleconference twenty months ago.

Dr. Maiello, the coal purchaser for Italy's largest steel company stated:

> "The second set of problems generates from the source of lack of cooperation, if I can use such expression, between the administration and the producers of coal, who keep advocating and granting sort of security to supply us coal and other actions which are taken at the same time which make very dangerous for potential or actual customers of American coal to stay in the American market. I'm referring to the freedom which has been given to basically two railroads to charge whatever tariff they want with no defense, no control whatsoever on the part of the monetary authorities." As you well know, most of the coal mines can only be served by one railroad, so we are, those two railroads are--have a monopoly against us, and the only defense we could have or we might have is just to step out of those mines, which is certainly not what is in the interest of the producing states." (emphasis added.)

And in respect to the relative costs/gains of improving domestic harbor depths vs. controlling railrates, Mr. Bogard, the fuel manager for Denmark's major electric utility stated:

> "On the other hand, dredging could be very costly to the United States, and you have to take the foot cost calculation before you decide that. If you take the mine price, it will be 25 U.S. dollars. The rate freight would be 17 U.S. dollars, and PANAMEX vessel will only cost $6.00 at the present market. So if you dredge you might save one or two dollars, but you still have the very high freight element from the rate growth of $17.00 and, therefore, unless you cope with the rate growth you won't be able to compete. That's the problem."

These conditions still exist. Despite small recent increases, coal exports remain at depressed levels. Meanwhile, coal imports have found their way into several U.S. coastal markets. In addition, the economic stage is set for coal imports to move inland to power plants on or near navigable waterways.

The Captive Shipper Problem Is Not Limited to Coal

Other bulk commodities, produced or shipped in the U.S., have the same captive problems with the railroads. Grain, fertilizer, chemicals, primary forest products and some perishable commodities, are largely obligated to the railroads for transportation.

Let me address one problem with respect to grain.

Recent studies by the State of Montana have demonstrated that the lack of long-distance transportation competition for grain shipments from Eastern Montana has resulted in excessive freight rates.

For example, some grain rates from Montana points to the Pacific North Coast return to the railroad $4.22 per car mile (PCM) compared to some points in Kansas, Nebraska and Colorado which return $2.61 PCM for hauls of the same distance. The difference: many shippers in Nebraska, Kansas and Colorado benefit from rail competition while growers and shippers in Montana have only one railroad to ship their goods. In addition, with rail abandonments brought about by mergers and railroad entry into ownership of grain elevators, further constrain the farmers' competitive options. The attached letter from the Montana Department of Commerce more fully explains the State's support for S. 447.

Options for Captive Coal Shippers and Producers

The options available for relieving the monopolistic grip of railroads in captive situations are limited, for example:

Regulatory Relief

While the ICC presumably maintains residual jurisdiction over rail rates charged captive shippers, this has not been exercised, in any meaningful way, over the last five to ten years. Rate increases imposed by the railroads, when appealed to the ICC, have rarely been denied. In short, the ICC has responded over the past decade, as if all rail rates were deregulated and has allowed marketplace factors to determine terms of service. This has been beneficial to both shippers and the railroads, only when inter- or intra-modal competition exists.

Duplication of Rail Facilities

Some rail rate relief for captive coal shipments was realized last year in one instance. This involved the conclusion of court proceedings between the BN and C&NW, which allowed joint rail operations on a joint line north to Coal Creek Junction, Wyoming. This line serves the southern-most part of the southern Powder River Basin coal field. Utility customers of several coal mines on this line have realized rail rate reductions of 30% from rates previously charged by the BN. These reductions are entirely attributable to the advent of competition along a relatively short stretch (about 100 miles) of 1,200-mile or more rail movement.

Additions to this existing line, through the construction of parallel rail facilities, are proposed in order to assure competitive service and rates to other mines in the southern Powder River Basin. Reportedly, this construction is proposed since the BN refuses to allow joint operations with another railroad on exclusive BN track.

The attached articles, from The Journal of Commerce, more fully reports on this situation.

Since the Staggers Act was passed, I believe this is the only instance of the proposed, purposeful duplication of rail facilities to serve captive shippers. The very limited application of this remedy reflects its inherent weaknesses: nearly prohibitive in cost, an inefficient use of capital, and continues an inflated delivered price of coal since the duplicate rail investment must be borne by one single class of users.

There is something askew, when our society requires the duplicate and wasteful investment in transportation facilities, in order to achieve the presumed benefits of competition in "common carriage". S. 447 would alleviate such folly if enacted into law.

Shutdown of Mines

Without the competitive pricing of rail freights provided in S. 447, the option available to all captive coal producers, is to cease, or substantially curtail, operations. While mine shutdowns, attributable to excessive transportation costs, have infrequently occurred over the last several years, they are becoming more prevalent. However, the curtailment of mining is widespread. Even though other marketplace and production factors have an impact on a mine's rate or level of output, captive transportation costs are the most determinant. For instance, only those coal operations in the Powder River basin with competitive rail service are producing at or near capacity. All other mines - those located with only one transportation option - are operating at a substantially reduced level.

Shutdowns will become more common in many instances as the remedy to captive rail transportation rates, causing infrastructure expenditures to be duplicated at sites where competition exists. A control of market area by inaction of the ICC rather than by free enterprise.

I've noted, in the case of Colowyo mine, of the reality of this option in the coming years. Other mines in the Western Colorado area are equally affected. It is my opinion that monopolistic freight rates were a major contributor to the recent near cessation of coal mining activities at several operations in western Colorado, where social impacts have been mitigated and infrastructure expenditures have been made.

I am not denying the normal marketplace shake-out among producers in times of low or depressed demand. These producer shake-outs are based on mining/operator efficiencies and quality of coal. They result from competition in the marketplace.

I do take exception though to the present situation, where the marketplace is dramatically skewed through the deregulation of a monopoly essential to the delivery of most coal produced.

Either this monopoly, the railroads, must be re-regulated or subjected to the same competitive forces (through enactment of S. 447) that face coal operators or other producers in the private sector.

The Alternative: Competitive Transportation

Our economic system depends on competition to establish rates, terms and availability of goods and services. However, in the delivery of essential facilities or services, which in and of themselves are natural monopolies, regulation is the historic method of setting availability and terms.

The only alternative to pervasive regulation of these facilities and services is intense competition.

Actually, under a scheme of simple deregulation of natural monopolies, larger monopolies and a higher degree of monopolization results.

In Railroads, The Free Enterprise Approach, Daniel Overbey addresses this point:

> "It first appears incongruous that deregulation, which was undertaken to increase railroad competition, should begin a trend toward eventual monopoly under two or three companies...When regulation is removed, competing firms in a natural monopoly will move, as if pulled by gravity, towards monopoly." (Page 101)

Actual evidence is supported by recent testimony before the Committee, on the proposed sale of Conrail to Norfolk-Southern, Mr. John Snow, President of the Chessie System Railroad, elaborated on the dangers of increased monopolies to shippers dependent on that (a single) system:

> "Railroads traditionally seek to reroute traffic over their long-haul routes. As long as competitive alternatives are available, this practice is generally desirable, and benefits shippers. But where one system controls both the origin and destination of the traffic, the results are extremely harmful. A railroad with that kind of control gains a dominant position over customers and competing railroads too." (Emphasis added.)(Page 11)

> "...Only those shippers open to competitive rail service at both the origin and destination points of their movements will be able to avoid the monopolizing grip of the NS-Conrail combination." (Page 12)

As the practical and workable alternative to the expansion of monopolization that has occurred over the last ten years of railroad deregulation, we support S. 447, since it imposes the potential of competition on the natural monopoly segments of railroads. This is far preferable to re-imposing a regulatory presence in an attempt to achieve fair rail rates.

The imposition of the potential for competition will have a salubrious effect on this essential service, such as:

- lower cost (most of which savings would be passed through to the customers);
- improve railroad efficiency (better utilization of capital employed);
- spur innovation and service.
- reverse loss of tonnage to other modes;
- increase rail-related job security.

The benefits of the competition, in contrast to reregulation, is supported by others. With the use of the term "open access" to include trackage rights on all rails, I again quote from Daniel Overbey :

> "With open access to all roadways, rail carriers could engage in true competition. Shippers would be given a choice among numerous rail service alternatives... Economic regulation would not be necessary for carriers since the ultimate regulator, the free market, would govern carrier competition. Common, contract, and private carriers would compete while sharing use of the roadway network." (Page 209)

Trackage Rights

The concept of trackage rights as an operational basis to assure competitive service, on a continuing basis, over private rail carrier lines, is well-established. Trackage rights are simply the ability for trains of one railroad to use the tracks of another railroad for reasonable rates. Trackage rights are commonly accepted by the railroad industry when they are convenient for them to do so. They have been in existence for a long time and they are granted every day by one railroad to another for the benefit of the railroads, not necessarily the shippers.

For instance, in the pending merger of the Sante Fe and Southern-Pacific Railroad systems, substantial trackage rights to assure competitive service have been proposed by both rail carriers as well as transportation consultants (The Woodside Group) to the State of California and the California Public Service Commission, as a condition of their support for the merger.

The Woodside Group recommended acceptance of the Rio Grande railroad request:

> "As a condition of the proposed SPSF merger, Rio Grande is seeking fee ownership, or an alternative grant of trackage rights, over Southern Pacific's lines (totaling 1,263 route miles) between Ogden and Roseville, CA, between Winnemucca, NV, and Klamath Falls, OR, and over four branch lines leading off those main lines. In addition, Rio Grande seeks unrestricted trackage rights over the following Southern Pacific lines (an additional 1,206 route miles)..."(emphasis added).

In addition, the Woodside Group recommends the acceptance of Union Pacific's trackage right request over several routes, including that from El Paso, Texas, to Colton, California (760 miles) and between Colton and Barstow-Lathrop, California (475 miles).

Certainly, it is reasonable to expect, that with the request and granting of trackage rights on such a scale as a condition of approving mergers, that trackage rights present no insurmountable operation or safety problems in the conduct of railroad business.

These, along with the current extensive use of trackage rights by railroads, are compelling examples which support the practical approach advanced in S. 447 to assuring competition.

The Antitrust Foundation

The principles underlying the statuatory approach to S. 447 are well founded. In a nutshell, if a monopoly railroad attempts to extract monopoly profits, it would have to open its tracks to competitors or else face treble damage action under the antitrust laws.

This premise has already been established by court decisions. For instance, the U.S. vs. Terminal Railroad Associates (1912). Most shippers of bulk commodities are captive to a railroad because that railroad has a "bottleneck" or "essential facility" monopoly. A business has a bottleneck or essential facility where it owns, operates or otherwise controls access to routing and equipment and is thus able to block access to the facility by potential competitors.

The courts have established that one who controls an essential facility can be guilty of monopolization. Four elements are necessary to establish liability under this theory:

1) Control of the essential facility by a monopolist;

2) A competitor's inability practically or reasonably to duplicate the essential facility;

3) The denial of the use of the facility to a competitor; and

4) The feasibility of providing the facility.

Therefore, the proposed amendment to the Sherman Act, verbalized in S. 447, simply serves primarily as a clarification of existing law. It defines a new antitrust violation but does so within the standards already established for the Sherman Act.

But, it is necessary to make this clarification to the Sherman Act because the railroads continue to argue that since the ICC exists and has some residual authority over them, parties injured by anti-competitive railroad activities have no right to claim damages under the anti-trust laws nor to any future relief in the form of an injunction. This immunity was established in a very important case (commonly referred to as 'Keogh') involving the Chicago and Northwestern Railway Company in 1920 after the ICC had been given complete authority to prescribe maximum and minimum rail rates.

Obviously, the railroads cannot be, and ought not be, both deregulated and exempt from a certain level of anti-trust damage. All we seek are simply rates and terms set by a competitive marketplace. In logic, it follows that those who oppose this suggestion are arguing for monopoly pricing or continuation of pervasive government regulation.

S. 447 simply requires the opening of essential facilities, through the option of trackage rights, where it is technically and commercially feasible to do so. The bill also mandates a reasonable rental for the use of any essential facilities and provides that no one can sue until he has offered the owner a fully compensatory return on its cost and investment and it has been rejected.

With the Staggers Act, Congress decided to deregulate rail carriers. This is a pattern followed with the trucking industry, the barge industry, the airline industry - why not the rail industry?

But, the thing that was overlooked by Staggers was the route monopoly held by the railroads. Because alternative essential facilities do not normally exist for the hauling of large bulk commodities, the trackage rights concept simply ensures the protection of an accessibility to a competitive marketplace as part and parcel of the Staggers Rail deregulation effort.

'One way to break the railroad monopoly would be to legislate universal trackage rights.'

By E.K. Olsen

The number-one problem that faces coal producers today is the reduced demand for coal. It is looked upon as being caused by several factors. However, the result of this problem is a lower volume of deliveries on contract sales, fewer, if any, sales in the spot market, and much greater competition among coal mines for possible sales.

Despite all the effort that has been placed, and continues to be stressed, on controlling our costs so that we may market our product, we find ourselves hobbled by the high expense of transporting our product to the customer. It is a problem over which we have no control, yet one which has shut down several coal mines around the nation. I get upset when my company loses a sale and I learn we were the lowest bidder, FOB mine, and end up one of the highest for the delivered product.

A typical example is a recent spot purchase of some 250,000 tons of coal by Central Power and Light Co. of Corpus Christi, Texas. Thirty-six mines were invited to bid. These mines are located in the eastern, western and central part of the U.S., as well as South Africa, Colombia, Australia and Canada.

CP&L advised me that we were the lowest bid FOB mine in Colorado, where our mine is located, but we came in 14th place in the delivered price at the utility's plant.

One company reported to me that a surface mine comparable to ours in size, located in the mountainous regions of British Columbia, could truck the same quality coal to a railhead and transport it to Vancouver, where it would be rehandled into ocean-going vessels. The coal then would be shipped around the west coast of North America, down and through the Panama Canal, then up through the Gulf of Mexico to Corpus Christi. It would be unloaded and transferred onto barges and barged 20 miles up canals to Victoria, Tex., where it would be unloaded onto the ground, reloaded into trucks, and trucked six miles into the plant and unloaded into the plant's stockpile.

The coal would be rehandled five to six times, transported by four intermodal means, and delivered at a lower cost than our coal loaded directly into a unit train and unloaded directly onto a conveyor belt feeding the plant. Yet, we had the lowest price FOB mine.

I get upset when my company loses a sale and...we were the lowest bidder, FOB mine.

Olsen

Incidentally, the cars of the unit train are owned by the utility, and the first 16 miles of the rail haul from our mine to the utility are owned by Colowyo Coal Co. at a capital investment of nearly $20 million.

Now, while the Staggers Act is worthwhile, it does not address the basic problem, which is the railroads' monopoly position. Could you imagine what airline tickets would cost you if there was only one carrier per route?

The difference between airlines and railroads is that airlines don't have a monopoly, but railroads do. Airlines don't own the airports, or the airways, but railroads own the tracks and the yards.

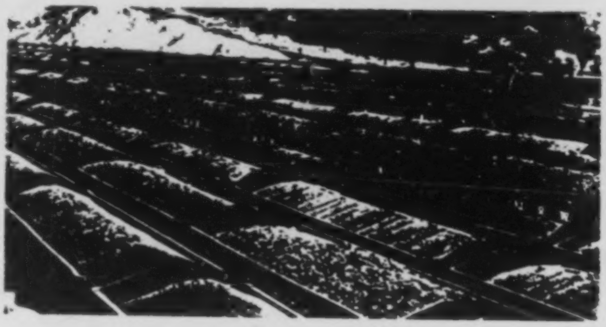
If this monopoly could be broken, railroads would compete with each other and the marketplace would set the freight rates just as it does in the airline business.

One way to break the railroad monopoly, in our opinion, would be to legislate universal trackage rights. Trackage rights now exist between several railroads, either as a result of regulatory action, or under contracts negotiated between certain carriers under which the railroads are allowed to use the tracks of other railroads in exchange for adequate compensation.

If this limited concept of trackage rights were made universal, there would be no monopoly. Any railroad, anywhere in the country, could compete for any coal or other commodity shipments just as any airline can compete freely anywhere within the country. With free competition, there would be no need for regulation of freight rates.

There was a bill being considered in the last Congress that would have been one way of achieving universal trackage rights and doing away with the present monopoly stranglehold the railroads have on shippers. This bill was introduced to "amend the Sherman Act to prohibit a rail carrier from denying to any shipper of certain bulk commodities with intent to monopolize use of its track, which affords sole access by rail to such shippers to reach the track of a competing railroad for the destination of the shipment."

Each person should urge his congressman, or any group of people having political influence, to push for this bill.



E.K. Olsen is president and general manager, Colowyo Coal Co., Meeker, Colo. This article is adapted from his opening remarks at the Coal Mining Session, Sept. 26, at the AMC Mining Convention in Phoenix.

December 12, 1984

W. R. GRACE & CO.
MINING DIVISION
STAPLETON PLAZA
3333 QUEBEC STREET, SUITE 8800
DENVER, COLORADO 80207
(303) 399-0779

May 28, 1985

Mr. Ken Starling
Counsel
Committee on the Judiciary
U. S. Senate
Washington, D. C. 20510

Dear Ken:

Thank you for discussing with me last week the issues surrounding S.447.

Your thoughts have provided additional insight on how the critical elements of this legislation can be better presented.

Enclosed please find my proposed answers to the questions sent following the April 23rd hearing.

Sincerely,

Ira E. McKeever
President - Western Coal Development

IEM:ab
Enclosures

1. QUESTION: How do you view the antitrust laws? What is it like to work under them?

ANSWER:

- I believe the Sherman-Clayton Acts are the most powerful statutory incentives protecting competition within our economic system.
- The antitrust laws, when applicable and enforced, assure bona fide competition among producers of goods and suppliers or services.
- The personal and corporate costs of being found in violation of the antitrust laws outweigh any potential gain:

Corporate costs include:

a) The potential for triple damages and other costs imposed by the court.

b) The disruption of business as well as the skewing of the allocation of resources required by the defense of court challenges under the antitrust laws.

c) The loss of senior manpower in the event of successful conviction.

d) Erosion of corporate standing and image in both business and consumer communities.

Personal costs include:

a) Potential jail sentence.

b) Loss of job.

c) Inability to get another job.

2. QUESTION: How do you think the provisions of S.447 will work on an actual basis, if adopted?

ANSWER: Under the present legislative proposal, competitive access or "trackage rights" can be exercised only if the sole facility carrier insists on a monopolistic freight rate for the use of its facilities. If the sole facility carrier matches or comes reasonably close to any competitive offer (or a pro-forma evaluation of the cost of providing the service by the shipper), then the sole facility owner provides the service.

A captive shipper would solicit bids from several railroads, including the sole facility owner. The competing railroads, based on their own experience, would have a basis to judge what a reasonable charge would be for the use of the tracks of the sole facility carrier. The shipper would then negotiate with the bidders and the sole facility owner to arrive at the lowest possible rate. If competitive bids were sufficiently lower than that of the owner-railroad, then the shipper would exercise the competitive access trackage rights provisions of S.447.

If trackage rights were exercised, the practical aspects of joint use of tracks and facilities that apply to current trackage situations would be controlling. Obviously, the competing or "guest" railroad would have adequately licensed engineers, trained crewmen and the like. An affirmative obligation for the appropriate equipment and its adequate maintenance would exist for the carrier performing the service. For instance, current practice requires the "guest" train to be crewed and equipped as are the owner-carrier trains so that the operational systems of the owner-carrier can be met. The "guest" train also receives the same priority and scheduling as the same or similarly configured trains of the owner carrier. Again, operational and safety considerations for the joint use of tracks or terminals by two or more carriers are satisfactorily resolved on an ongoing basis under current railroad practices.

Trackage rights are sufficiently accepted by railroads and successful in assuring competitive service that they are often mandatory conditions of mergers in order to address the anti-competitive aspects of mergers. For instance in the pending Santa Fe - Southern Pacific merger, it appears the California Public Service Commission will recommend the approximately 2,400 miles of trackage rights be granted the D&RGW to assure competitive service from Utah through Northern and Central California, and that nearly 800 miles of trackage rights be granted the Union Pacific from El Paso, (Texas) to Los Angeles in order to assure competitive service across the southwest and Southern California.

I believe that virtually all rates and terms of service for captive shippers will be determined through negotiation with the railroads. Few situations will go to trial under the antitrust laws. S.447 makes the provisions of the Staggers Act which allow the negotiation of rail rates to be fairly applied in captive as well as competitive situations.

**Colorado-Ute
Electric Association, Inc.**

P O Box 1149
Montrose, Colorado 81402
(303) 249-4501

Testimony of Colorado-Ute Electric Association
Prepared by Jerry C. Kempf
Director of Governmental Affairs

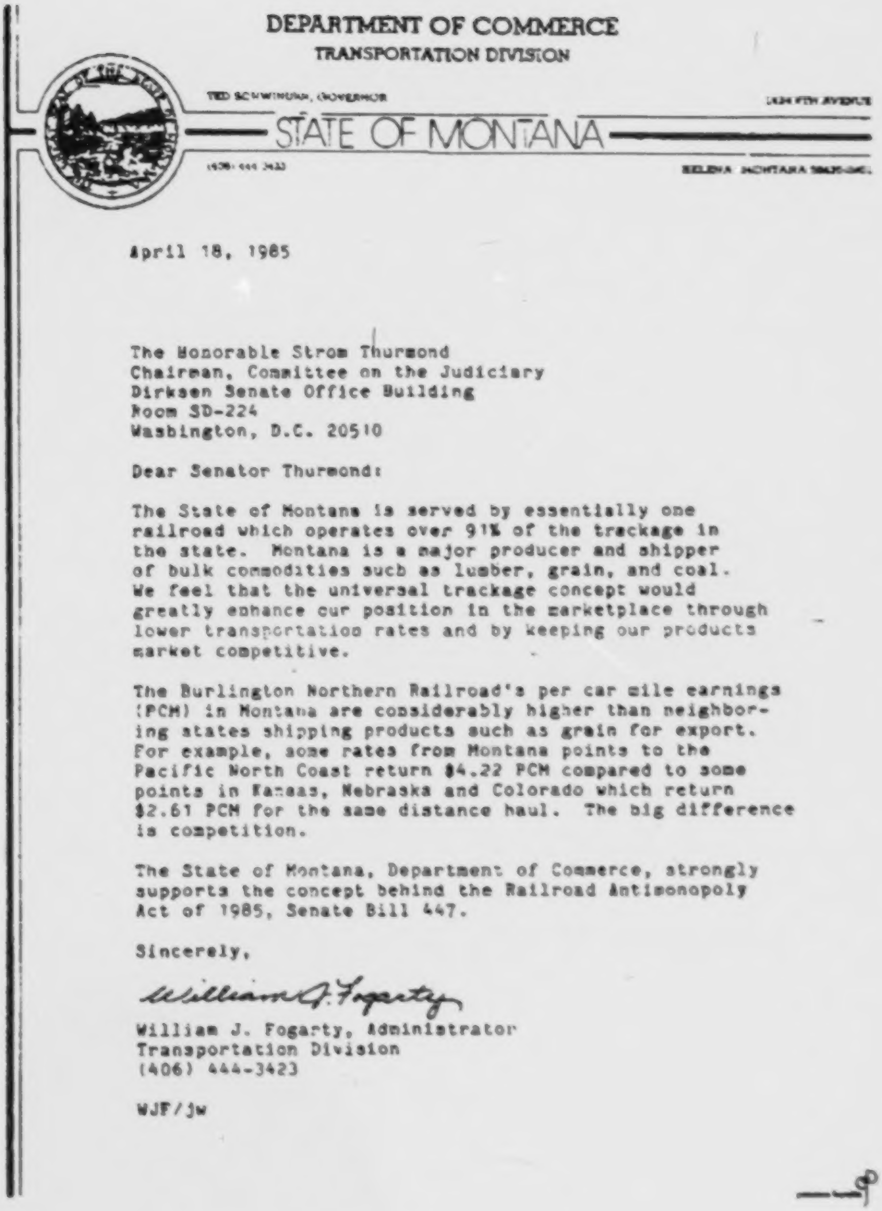
Gentlemen:

Colorado-Ute is a rural electric generation and transmission cooperative that serves 180,000 meters in Western Colorado. The largest portion of Colorado-Ute's electric sales are generated by pulverized coal combustion units. Colorado-Ute is the largest single Colorado user of Colorado coal.

While Colorado-Ute has been successful recently in negotiating freight contracts with the railroads, this has not always been the case. In our opinion, a large part of the problem in entering into successful negotiations for rail freight has been the protection of the railroad by its regulatory body the ICC. Rarely is a railroad found to be revenue sufficient by the ICC, which is difficult to believe. Consequently, the railroad in the "captive shippers" situation has a tremendous effect on the total cost of coal delivered to the point of use. We feel that a total deregulation of the railroads would be the simplist, cleanest and fairest solution to all involved. Antitrust provisions that currently exist in todays law in the Sherman and Clayton Acts would prevail and competition in railroad pricing would be resolved.

We have advocated deregulation in our own industry, acknowledging the existance of exactly the same controls and we feel that a complete deregulation in this situation is the most sensible solution.

Thank you very much for your consideration of our comments on this issue. We trust your deliberations will result in action that will bring fairness in pricing to all shippers needing to use rail lines to transport their product.



DEPARTMENT OF COMMERCE
TRANSPORTATION DIVISION

TED SCHWINDEN, GOVERNOR
1424 9TH AVENUE
STATE OF MONTANA
(406) 444-3423
HELENA, MONTANA 59620-0401

April 18, 1985

The Honorable Strom Thurmond
Chairman, Committee on the Judiciary
Dirksen Senate Office Building
Room SD-224
Washington, D.C. 20510

Dear Senator Thurmond:

The State of Montana is served by essentially one railroad which operates over 91% of the trackage in the state. Montana is a major producer and shipper of bulk commodities such as lumber, grain, and coal. We feel that the universal trackage concept would greatly enhance our position in the marketplace through lower transportation rates and by keeping our products market competitive.

The Burlington Northern Railroad's per car mile earnings (PCM) in Montana are considerably higher than neighboring states shipping products such as grain for export. For example, some rates from Montana points to the Pacific North Coast return $4.22 PCM compared to some points in Kansas, Nebraska and Colorado which return $2.61 PCM for the same distance haul. The big difference is competition.

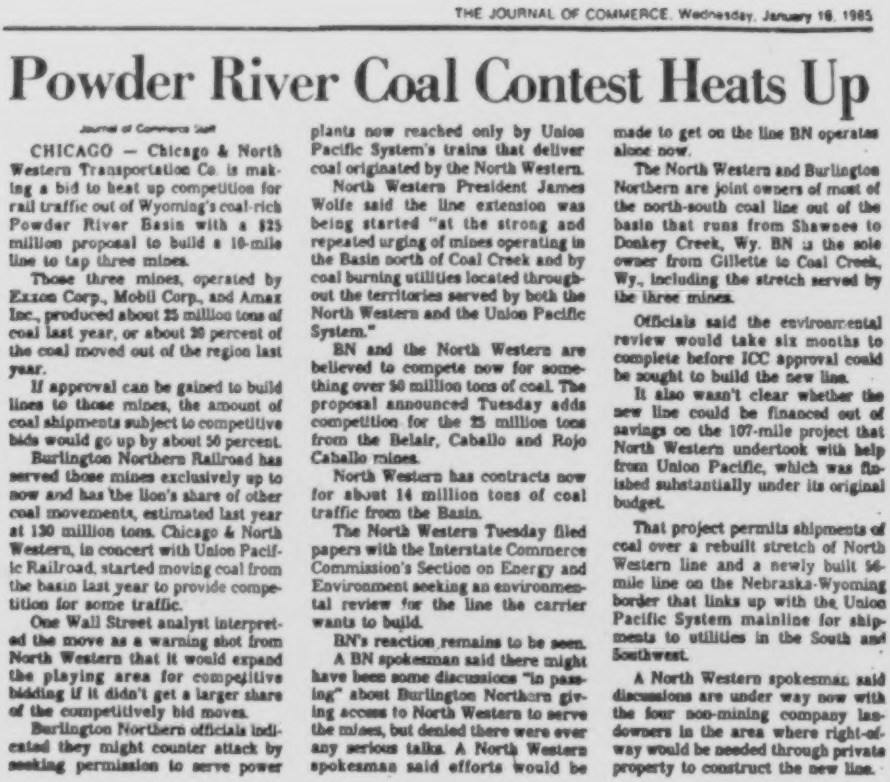
The State of Montana, Department of Commerce, strongly supports the concept behind the Railroad Antimonopoly Act of 1985, Senate Bill 447.

Sincerely,

William J. Fogarty

William J. Fogarty, Administrator
Transportation Division
(406) 444-3423

WJF/jw



THE JOURNAL OF COMMERCE, Wednesday, January 16, 1985

Powder River Coal Contest Heats Up

Journal of Commerce Staff

CHICAGO — Chicago & North Western Transportation Co. is making a bid to heat up competition for rail traffic out of Wyoming's coal-rich Powder River Basin with a $25 million proposal to build a 10-mile line to tap three mines.

Those three mines, operated by Exxon Corp., Mobil Corp., and Amax Inc., produced about 25 million tons of coal last year, or about 20 percent of the coal moved out of the region last year.

If approval can be gained to build lines to those mines, the amount of coal shipments subject to competitive bids would go up by about 50 percent.

Burlington Northern Railroad has served those mines exclusively up to now and has the lion's share of other coal movements, estimated last year at 130 million tons. Chicago & North Western, in concert with Union Pacific Railroad, started moving coal from the basin last year to provide competition for some traffic.

One Wall Street analyst interpreted the move as a warning shot from North Western that it would expand the playing area for competitive bidding if it didn't get a larger share of the competitively bid moves.

Burlington Northern officials indicated they might counter attack by seeking permission to serve power plants now reached only by Union Pacific System's trains that deliver coal originated by the North Western.

North Western President James Wolfe said the line extension was being started "at the strong and repeated urging of mines operating in the Basin north of Coal Creek and by coal burning utilities located throughout the territories served by both the North Western and the Union Pacific System."

BN and the North Western are believed to compete now for something over 50 million tons of coal. The proposal announced Tuesday adds competition for the 25 million tons from the Belair, Caballo and Rojo Caballo mines.

North Western has contracts now for about 14 million tons of coal traffic from the Basin.

The North Western Tuesday filed papers with the Interstate Commerce Commission's Section on Energy and Environment seeking an environmental review for the line the carrier wants to build.

BN's reaction remains to be seen.

A BN spokesman said there might have been some discussions "in passing" about Burlington Northern giving access to North Western to serve the mines, but denied there were ever any serious talks. A North Western spokesman said efforts would be made to get on the line BN operates alone now.

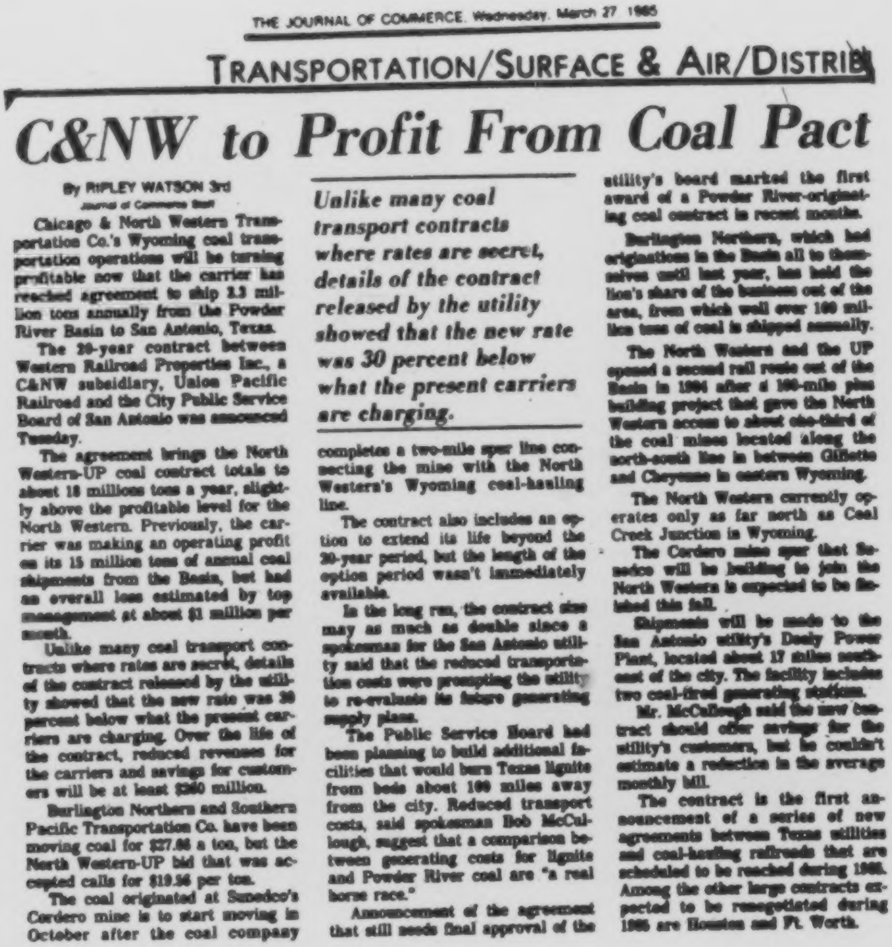
The North Western and Burlington Northern are joint owners of most of the north-south coal line out of the basin that runs from Shawnee to Donkey Creek, Wy. BN is the sole owner from Gillette to Coal Creek, Wy., including the stretch served by the three mines.

Officials said the environmental review would take six months to complete before ICC approval could be sought to build the new line.

It also wasn't clear whether the new line could be financed out of savings on the 107-mile project that North Western undertook with help from Union Pacific, which was finished substantially under its original budget.

That project permits shipments of coal over a rebuilt stretch of North Western line and a newly built 56-mile line on the Nebraska-Wyoming border that links up with the Union Pacific System mainline for shipments to utilities in the South and Southwest.

A North Western spokesman said discussions are under way now with the four non-mining company landowners in the area where right-of-way would be needed through private property to construct the new line.



THE JOURNAL OF COMMERCE, Wednesday, March 27 1985

TRANSPORTATION/SURFACE & AIR/DISTRIB

C&NW to Profit From Coal Pact

By RIPLEY WATSON 3rd
Journal of Commerce Staff

Chicago & North Western Transportation Co.'s Wyoming coal transportation operations will be turning profitable now that the carrier has reached agreement to ship 3.3 million tons annually from the Powder River Basin to San Antonio, Texas.

The 20-year contract between Western Railroad Properties Inc., a C&NW subsidiary, Union Pacific Railroad and the City Public Service Board of San Antonio was announced Tuesday.

The agreement brings the North Western-UP coal contract totals to about 18 millions tons a year, slightly above the profitable level for the North Western. Previously, the carrier was making an operating profit on its 15 million tons of annual coal shipments from the Basin, but had an overall loss estimated by top management at about $1 million per month.

Unlike many coal transport contracts where rates are secret, details of the contract released by the utility showed that the new rate was 30 percent below what the present carriers are charging. Over the life of the contract, reduced revenues for the carriers and savings for customers will be at least $260 million.

Burlington Northern and Southern Pacific Transportation Co. have been moving coal for $27.86 a ton, but the North Western-UP bid that was accepted calls for $19.56 per ton.

The coal originated at Sunedco's Cordero mine is to start moving in October after the coal company completes a two-mile spur line connecting the mine with the North Western's Wyoming coal-hauling line.

Unlike many coal transport contracts where rates are secret, details of the contract released by the utility showed that the new rate was 30 percent below what the present carriers are charging.

The contract also includes an option to extend its life beyond the 20-year period, but the length of the option period wasn't immediately available.

In the long run, the contract size may as much as double since a spokesman for the San Antonio utility said that the reduced transportation costs were prompting the utility to re-evaluate its future generating supply plans.

The Public Service Board had been planning to build additional facilities that would burn Texas lignite from beds about 100 miles away from the city. Reduced transport costs, said spokesman Bob McCullough, suggest that a comparison between generating costs for lignite and Powder River coal are "a real horse race."

Announcement of the agreement that still needs final approval of the utility's board marked the first award of a Powder River-originating coal contract in recent months.

Burlington Northern, which had originations in the Basin all to themselves until last year, has held the lion's share of the business out of the area, from which well over 100 million tons of coal is shipped annually.

The North Western and the UP opened a second rail route out of the Basin in 1984 after a 100-mile plus building project that gave the North Western access to about one-third of the coal mines located along the north-south line in between Gillette and Cheyenne in eastern Wyoming.

The North Western currently operates only as far north as Coal Creek Junction in Wyoming.

The Cordero mine spur that Sunedco will be building to join the North Western is expected to be finished this fall.

Shipments will be made to the San Antonio utility's Deely Power Plant, located about 17 miles southeast of the city. The facility includes two coal-fired generating stations.

Mr. McCullough said the new contract should offer savings for the utility's customers, but he couldn't estimate a reduction in the average monthly bill.

The contract is the first announcement of a series of new agreements between Texas utilities and coal-hauling railroads that are scheduled to be reached during 1985. Among the other large contracts expected to be renegotiated during 1985 are Houston and Ft. Worth.

Senate McConnell. Our next witness is Mr. William Dempsey, president of the Association of American Railroads.

STATEMENT OF WILLIAM H. DEMPSEY, PRESIDENT, ASSOCIATION OF AMERICAN RAILROADS, WASHINGTON, DC

Mr. Dempsey. Mr. Chairman, thank you very much. I appreciate being able to be here and present the views of the railroad industry on this bill. And I would ask that my statement be incorporated in the record.

Senator McConnell. Without objection, that will be done.

Mr. Dempsey. The industry, as the committee is aware, is strongly opposed to this legislation. In the few minutes that I have before the committee, I would like to make three points.

The first is that there is no need for the legislation, no factual basis for it much for the same reason that Mr. Rule suggested.

Second, there is a collision between the bill and well accepted principles of the antitrust laws. I think I need not tarry on that point. It has already been covered fully by Mr. Rule and by Mr. Donovan, and I would simply adopt what they have said about the defects of the bill in that respect. It is not a bill based on monopolization because it disregards altogether, for example, intermodal competition—competition from trucks and barges, and our industry is characterized by pervasive competition of that sort. A study made for the Interstate Commerce Commission concluded that 85 percent or more of rail traffic is subject to competition.

And third, there is a collision between this act and the Staggers Act that was enacted by the Congress in 1980.

As to the need for the legislation, the concentration, I take it, from what I have heard, has been on coal rates. It has been suggested by Mr. McKeever and others that in the wake of Staggers there has been an explosion of coal rates, that the Commission does not control the rates, and that that calls for congressional intervention.

Here are the facts, and I am giving you Bureau of Labor Statistics figures. In the last 3 years under Staggers, the railroad coal rates increased in total by only 6.6 percent as compared with an 8.1 percent increase in railroad inflation and a 7 percent increase in total railroad rates.

In other words, coal rates have actually gone down in real dollar terms in the last 3 years and they have risen in dollar terms less than our average rates have gone up, and that pattern extends back for a dozen years.

Since 1972, discounted for inflation, our coal rates have gone down 1 percent, and this is during a period in which coal prices at the mine mouth have gone up in real dollar terms about 20 percent.

Senator McConnell. With all due respect, I think you would have a hard time convincing a lot of eastern Kentucky coal shippers of that.

Mr. Dempsey. Well, let me say this, Mr. Chairman, I can speak only in general terms, of course. I can give you only the national statistics, and I am in no position to say that in a particular case there might not have been a run up in coal rates that the Commission might ultimately determine has been unreasonable.

But this is the general pattern, and what it does suggest strongly is that if there have been some cases of unreasonable escalation of coal rates, they are not pervasive. Of course, there are rates above the average, and there are rates below, but there is certainly no systematic abuse by the railroad industry of the powers, the rights that they have been given in the Staggers Act. I think that remains to be demonstrated and, in my judgment, it cannot be demonstrated.

Let me pass then to the question of the Staggers Act. There is no lacuna here contrary to what Mr. Donovan says. The Staggers Act was passed in order to put the railroad industry back on some decent economic footing.

At that time, we had seen the collapse of the entire eastern part of the United States in terms of rail shipping. The blight had spread to the Middle West and the Rock Island bankruptcy and the Milwaukee Road. Some 20 percent of the rail industry was in bankruptcy. Something radical had to be done, and so we had the most important piece of rail legislation in this century in the Staggers Act.

But it was recognized by the Congress that rate regulation for the captive shipper had to be maintained, and that is the basic premise of the Staggers Act—that there should be no regulation where there is competition, but where there is no competition, or effective competition within the terms of the act, that rate regulation by the Commission should continue.

Now, there had been criticisms leveled by us as well as by shippers about the way the Commission has approached this responsibility, which, after all, it always has had. And, it is true that no one at the present time can know what will be the final standards promulgated by the Commission with respect to the regulation of coal.

They may not fully satisfy the shippers. They may not fully satisfy the railroads, but it is time enough to look at those regulations when they are promulgated. Then, I suggest that if there is anything wrong with them and if the courts do not overturn whatever flaws there are in them that the appropriate way of dealing with that problem, is, as Mr. Rule suggested, the same say that the Congress has always dealt with the railroad industry and regulation of the railroad industry and that is by oversight of the Commission under the Staggers Act principles.

The collision with the Staggers Act is manifest. I think that Mr. Donovan really suggested it when he pointed out, for example, that under the Staggers Act, the Commission is charged expressly in terms of its regulatory decisions, with attempting to assist the railroad industry in obtaining revenue adequacy. That is, as he points out, an important social policy. It was expressly adopted by the Congress in the Staggers Act. It would obviously be disregarded by the Courts in whatever kind of rate regulation they would engage in pursuant to the antitrust laws. That is a flat undermining of one of the most important principles adopted by the Congress in the Staggers Act.

Now, let me give you simply one more example of the kind of conflict that would arise. The Staggers Act expressly recognizes the validity of what we call differential pricing—that is, pricing according to the level of demand for different products and that depends in large measure upon the amount of competition with respect to different products that are being shipped.

The principle of differential pricing has been recognized by the Commission and the courts for decades, and as I say, is expressly recognized in the Staggers Act as essential to the well-being of the industry. Now, consider what happens under this bill. An offer of trackage rights must be made, both to railroads that connect and to shippers. What happens if the offer is declined, as it very often would be for perfectly sensible commercial reasons?

What happens then under the act, is that the railroad is precluded from differential pricing. All pricing must be essentially on a cost equal basis. That would lead to this result—it would be ruinous to the railroad and it would be very, very harmful to the captive shipper for this reason. Let us assume that we have two types of traffic being carried; one that is highly competitive with trucks. We charge, let us say, 120 percent of variable costs, and we make more than our variable costs, but less than our fully allocated costs. This traffic is still beneficial because that excess goes to defray part of our fixed costs, so that the whole burden does not fall on the captive shipper. Now, what do we do if we cannot differentially price?

We could either price the coal down to the competitive commodity level but that would be certain ruination because we would not be covering anything like our fully allocated costs. The only other option would be to price the competitive traffic up to the captive traffic, that would lead, of course, to the loss of the competitive traffic. It would shrink the revenue base, it would impose more of a burden on the captive shipper, but it would be the industry's only chance.

So we would have then a collision between the Interstate Commerce Commission, which would approve this sort of rate making, and this statute that would impose antitrust liability upon the railroads if they engaged in that very type of pricing that has been approved by the Congress and is approved by the Interstate Commerce Commission.

Thank you, very much, Mr. Chairman.

Senator McConnell. Thank you.

Questions?

Mr. Feidler. Mr. Dempsey, you are quoted in the January 2 edition of the Journal of Commerce as saying in regards to the Sherman Act, "The railroads are prepared to live under the same laws that govern other business."

And at the recent Conrail hearings many of the rail executives that testified said somewhat similar things—that they were prepared to live under the laws, like everybody else.

However, from earlier witnesses, we have heard that possibly the antitrust laws are not fully applicable to the railroads. For instance, you are not subject to treble damages and you are not subject to injunctive relief from shippers. Are there any constructive changes to the antitrust laws, as they pertain to railroads, that you could agree to or that you would recommend to this committee?

Mr. **Dempsey**. Oh, I think that is a very good question because you are quite right, I have said this from time to time and other chief executives of the industry have taken the same view.

We really do want to be treated as much as possible like other American industry. We have suffered for a long time, under what we consider to be, in effect, discriminatory treatment by agencies as well, I must say with all respect, by legislative bodies. We lost, as you know, in the wake of the Staggers Act, our most important antitrust immunity. We lost the rate bureaus and therefore, the ability for the industry to fix prices collectively. We knew that we would have to pay that price if we were to get significant deregulatory relief.

Now, I am a long way from antitrust practice, a good dozen years, and so I am not sitting right here today, competent to speak to the question that Mr. Rule spoke to and then Mr. Donovan spoke to. My understanding has always been that we are subject to sections 1 and 2 of the Sherman Act. But that there may be still remaining questions as to what sort of implied immunity that we may have because of pervasive regulation by the Interstate Commerce Commission.

My impression is that those are difficult questions that depend upon the facts of the particular case. In that respect, we would be the same as other industries that are still, to a significant extent regulated. That is to say, the courts are left with the obligation of determining whether or not there is a conflict between the remaining regulation and the jurisdiction of the antitrust courts.

So I would not be prepared to give up the opportunities that the other industries have to make those arguments. Now, if there is any other aspect of the antitrust laws that we could constructively suggest a change on, even to our detriment, I will certainly review that, and respond.

Mr. **Feidler**. Thank you, Mr. Dempsey.

Mr. Chairman, we had some other written questions, if possible, we would like to submit to Mr. Dempsey.

Senator **McConnell**. That will be fine, will you respond to those?

Mr. **Dempsey**. Surely.

Senator **McConnell**. Thank you very much.

[Prepared statement, along with the responses to 19 questions submitted by Senator DeConcini, follow:]

STATEMENT OF WILLIAM H. DEMPSEY
PRESIDENT OF THE ASSOCIATION OF AMERICAN RAILROADS

I welcome this opportunity to express the views of the Association of American Railroads on S. 447, a bill "To amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its tracks which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment and to apply Clayton Act penalties to monopolizing by rail carriers."

The purpose of the bill is said to deal with the perceived problem of the "captive" shipper. See remarks of Senator DeConcini, Cong. Rec., February 7, 1985, S. 1341-42. The bill would superimpose the judicial remedies of the antitrust laws, without the factual and legal defenses normally associated with such laws, over the carefully structured checks and balances found in the Interstate Commerce Act. What would result, in practical effect, would be duplicative and unnecessary maximum rate regulation.

We believe that Congress ought not to abandon the objectives it achieved in 1980 with passage of the Staggers Rail Act. With deference, we consider that S. 447 would saddle railroads with a new set of rules, poorly suited to the factual environment of the transportation industry, in order to redress grievances that cannot be substantiated on the facts.

A review of the provisions of the bill will show the hardships -- unnecessary, in our judgment -- it would visit upon an industry just beginning to emerge from decades of government handicapping. When these provisions are laid alongside the existing matrix of the Interstate Commerce Act and judged against the facts, we submit a compelling case exists for maintaining the freedoms written into that law by the Staggers Act. Contentions that those freedoms have led to abuse simply do not stand up.

Provisions of S. 447. The bill deals with the case of a railroad which owns the only rail facility serving all or any part of a movement of "bulk commodities," as defined in the bill.

Under Section 3 of the bill (proposed section 9(a)(1) of the Sherman Act), such a railroad is presumed to be an unlawful monopoly. This is the case without the need for anyone to establish that the situation actually affects, reduces or threatens to lessen competition. A railroad which for historical or geographical reasons has a sole facility would now be faced with the full array -- civil and criminal -- of the antitrust weapons, without any opportunity to defend itself on the facts or on the law.

This legislation permits a railroad owner to purge itself of this presumed monopoly by electing one of two confiscatory alternatives. Under S. 447, if a shipper or another rail carrier seeks the use of a sole facility, the railroad owner has no choice but to open its facilities for a rental to be set by vague and uncertain standards, or to subject itself to maximum rates set in accordance with a proportional cost formula. Costly and uncertain litigation will lie ahead whatever the choice. If the facilities are opened under a trackage rights arrangement, lawyers will feast over the meaning of "generally accepted principles regarding just and reasonable rental of track." If this avenue is not chosen (or even if it is, but other railroads do not elect to compete), the owning railroad cannot establish a rate above a level that "would yield a fair return on the proportion of the owner rail carrier's prudent investment in the sole railroad facility that the shipper's traffic bears to all traffic using such sole railroad facility." Every operative word in the quoted portion is an invitation to litigation.

While S. 447 has all the coercive features of the antitrust laws, it has none of their safeguards. The railroads face pervasive competition, and the Congress so found when it enacted the Staggers Rail Act. Even where rail-to-rail competition does not exist, intermodal, product or geographic competition usually does. Under the bill, the fact that such competition existed would be irrelevant. Thus, a shipper of perishable commodities served by one railroad could compel a grant of trackage rights to a second railroad even though most of its produce moved to market by truck. And this is not a far-fetched hypothetical -- perishable commodities were exempted from regulation because, among other reasons, the I.C.C. found that trucks had 90 percent of the market for transportation.

Although it carries some of the trappings, S. 447 is plainly not an antitrust bill; it is a bill to impose a cost-based maximum rate standard on the railroad industry without explicitly amending the Interstate Commerce Act. Indeed, the measure flies in the face of the finding the Congress made in 1980 -- that "today, most transportation within the United States is competitive." This conclusion is no less true in 1985, and its thrust should not be blunted by an unsupported presumption of monopoly power. A procedure for determining the state of competition with respect to any particular rail shipment is the cornerstone of maximum rate regulation under the Interstate Commerce Act and the safeguards of that Act should not be short-circuited.

Present Law. Railroads are already subject to the antitrust laws if they engage in predatory or anticompetitive pricing or practices. Any substantive comfort the railroad industry found in the Reed-Bulwinkle Act of 1948 (49 U.S.C. 5(b)) with respect to collective ratemaking was removed by the I.C.C. in implementing the Staggers Act. And, with respect to any use or abuse of monopoly power through ratemaking, the railroads remain fully regulated by the I.C.C.

I would like to review the ways in which the Interstate Commerce Act, as amended by Staggers, deals with these issues of competition and rate regulation. This review will establish that the system works and need not be fixed.

A comprehensive and exclusive statutory scheme for regulating rail rates and for compelling a railroad to permit the use of its facilities by another in situations where that was appropriate was completed with the Transportation Act of 1920. With the Staggers Rail Act of 1980, Congress loosened the reins on ratemaking that had been applied in that earlier era of our economic life, but it did not remove them. While recognizing that reasonable rates for rail transportation should be set by "competition and the demand for services" to the maximum extent possible, the national policy reformulated in the Staggers Act also recognized as an objective of regulation the need "to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and to attract capital."

The concept of limiting the Interstate Commerce Commission's jurisdiction to regulate the maximum reasonableness of rates originated with the 4-R Act of 1976. It limited the Commission's jurisdiction to instances where the rail carrier was shown to have "market dominance," which was defined as an "absence of effective competition." The Staggers Act gave meaning to this provision by further modifying the definition of market dominance to remove from the Commission's jurisdiction rates which yielded a revenue-to-variable cost percentage below a prescribed threshold -- currently 180 percent.

As a result of these two amendments to the Interstate Commerce Act, the Commission now has jurisdiction to determine the reasonableness of any rail rate where the yield from that rate is above 180 percent of variable cost and where there is an absence of effective competition. In assessing the absence or effectiveness of competition the Commission looks at all aspects of competition -- intramodal, intermodal, product and geographic.[1]

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[1] These terms are used to mean, respectively, competition among railroads, competition between a railroad and another mode of transportation, competition arising from the substitutability of products, and competition arising from the availability of the same product from different sources or the ability to ship the product to different destinations.

Thus, while there has been deregulation of rail rates where those rates are found to be effectively constrained by competition, there has been no deregulation of rates where the Commission finds an absence of effective competition.[2] In that circumstance the Commission retains the exclusive power it has always had to prescribe maximum rate levels.

It is important to note in this respect that the amendments effected by Staggers require the Commission, in determining the maximum reasonableness of rates, to consider the revenue needs of the rail carrier. This admonition sprang from the fact that the hand of regulation rested heavily against the industry long after the railroads had lost their historic monopoly. The railroads suffered precipitous declines in the years following World War II. Between 1970 and 1979, over 20% of the railroad industry had gone into bankruptcy as a result of years of inadequate earnings. Nationalization occurred in the Northeast and capital starvation menaced the viability of the entire industry. Congress realized a privately-owned railroad industry could no longer be used as an instrument of national policy to subsidize other industries or regions. It had to be regulated in accordance with sound economic principles following as much as possible the dictates of a free market. At the very least, that meant that over the long run the railroads had to be allowed to earn adequate returns on the capital invested in the business. S. 447, on the other hand, trashes the legislative history of the Staggers Act.

The point I wish to stress with respect to S. 447 and the concerns of this Committee is this: The bill under consideration deals with situations in which a shipper has access only to a single railroad -- where the shipper is "captive," in popular parlance -- and would set ratemaking standards for those situations.[3] But the Congress has for decades entrusted regulation of rail ratemaking to the Interstate Commerce Commission, and as recently as 1980, enacted a comprehensive reform of the regulatory system dealing precisely with the subject of S. 447 -- the standards to be applied in determining which shippers are truly "captive" and in determining the lawfulness of rates charged to such shippers. Thus there is no lacuna to be filled by the antitrust laws. Rather, the remedies afforded by the Interstate Commerce Act are plainly exclusive. It would be grossly unfair to enact a measure under which a railroad, having successfully established before the Commission and the courts that its rate to a so-called "captive" shipper was reasonable under the Interstate Commerce Act, could then be compelled to pay treble damages to that shipper pursuant to a finding that the rate was unlawful under the antitrust laws.

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[2] In conformity with this principle, before the Commission may completely exempt a type of service from regulation pursuant to its authority under 49 U.S.C. 10505, it must find with respect to that service that regulation "is not needed to protect shippers from the abuse of market power."

If there are concerns about certain areas of railroad regulation, they should be addressed within the regulatory context, giving full consideration to all of the complicated economic issues, and not by asking the courts which are neither specially trained nor equipped to resolve those issues -- to act as super regulators under the antitrust laws.

The inappropriateness of the proposed legislation is compounded by the fact that it would seek to resolve perceived (but, we submit, overstated and, indeed, largely non-existent) problems by turning them over to the courts rather than the administrative body which Congress created for the purpose of regulating railroads and which has done so for nearly 100 years. There is certainly no demonstrated necessity for so drastic a step. And one result -- the shifting of workload from the Commission to the courts with increased probability of inconsistent decisions -- is certainly not a desirable public policy objective.

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[3] It is to be noted that the bill is fatally flawed under economic and antitrust analysis because it ignores the availability of non-rail transportation and other economic constraints on rail pricing decisions which are frequently, if not inevitably, present in the situation addressed by the bill.

Rail regulation was entrusted to the I.C.C. by the Congress because Congress recognized that the economic complexities of a sound national rail transportation policy were such that its administration required a special expertise which the courts do not possess and should not exercise as a matter of initial jurisdiction. That is still true. We recognize that there have been concerns expressed regarding Commission actions. But enactment of a special railroad section of the antitrust laws is not the appropriate response. These concerns can and should be addressed within the regulatory framework which is designed to give full consideration to the complexities involved in implementing a national policy to develop and maintain a sound, long-term rail transportation system.

One of the prime needs of that system is the ability to price services based on the demand for those services -- sometimes termed "differential" pricing. In my testimony before this Committee last September on S. 2417, a bill very similar to S. 447, I discussed the concept of, and need for, differential pricing at some length. Rather than repeat the discussion at this point, I have appended an excerpt from my prior testimony. Suffice it here to note that a railroad, like any other enterprise, needs to recover its full costs (variable costs plus fixed costs). For competitive reasons, a large amount of traffic will move by rail only if rates are set below full cost but not below variable cost -- thus making some contribution to fixed costs. Because of that contribution, the rates for less competitive traffic -- i.e., for the more rail-dependent or "captive" shipper -- are lower than they would be were the competitive traffic moving by truck or barge. Thus, differential pricing is not a subsidy to competitive traffic but a benefit to "captive" traffic.

The bill's objective is to limit severely the range within which a railroad could differentially price its services by imposing intramodal competition through the grant of trackage rights or, failing that, through a prescribed maximum rate ceiling.

Let's look now at what would likely happen if a railroad were compelled to grant trackage rights on the terms specified in the proposed section 9(a)(2), i.e., "in accordance with generally accepted principles regarding just and reasonable rental of track." There are no "generally accepted principles" that I am aware of other than the requirement for fair and just compensation imposed by the Constitution. Fair and just compensation is generally measured by fair market value.

In this hypothetical case, the return the railroad earns on its investment in the marketplace is the measure of its value. Thus, any rental term less than the capitalized value of the revenue the property is producing (or capable of producing) at the time of the taking would be an unlawful taking of property without due process. As a result, a railroad paying for trackage rights at fair market value would, in all likelihood, be required to set rates at or near the previously prevailing level. In that event, the so-called "captive" shipper would have gained nothing in the process.

If the trackage rights alternative is unsatisfactory, the maximum rate standard of proposed section 9(a)(3) fares no better. That standard would require that maximum rate levels for bulk commodities be set on a proportion-of-full cost basis. That forces the railroad to lose money. Assume that the traffic on the rail plant is divided equally between the bulk commodity in question -- and that this traffic is truly captive -- and competitive traffic. The competitive traffic would be lost if the railroad attempted to price it on a full pro rata cost basis; as a result, the rates for that traffic are set lower than that for the captive traffic but nevertheless cover something above variable costs -- thereby benefitting the captive traffic by defraying part of the fixed costs. Under S. 447, the railroad could not raise the rates on competitive traffic without losing that traffic. As a result, a percentage of its fixed costs would either not be covered -- an invitation to bankruptcy -- or the captive shipper would become the only remaining customer to bear all of the fixed costs on the line, everyone else having gone to the competition.

Thus, under the formula proposed in section 9(a)(3), no one wins. The competitive traffic loses because it pays a higher rate to a truck or water carrier for transportation it could have gotten at a lower rate from a rail carrier under differential pricing. The less competitive, or "captive," traffic loses because rates are higher than they would have been under differential pricing. And, ultimately, the railroads would lose because in reality a truly "captive" shipper is a rare bird. As in all other areas of our economy, the demand for rail service varies across the spectrum of that service; and, as prices go up, more and more shippers seek and find alternatives. Eventually, there would not be enough shippers left to support rail services.

The lesson is a familiar one; someone has to pay the full cost of providing rail service. If it is not to be the taxpayer then it must be the shippers. Differential pricing spreads this responsibility as broadly as possible. By barring differential pricing, section 9(a)(3) would impose this responsibility upon "captive" shippers alone -- a burden that it is unlikely they would be able or willing to bear.

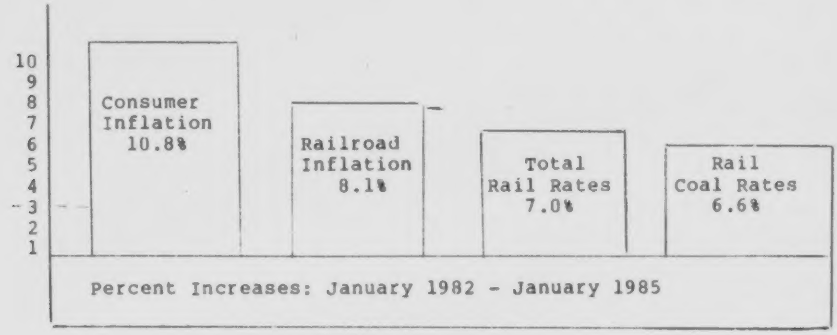
All that I have said is not to deny, but rather to recognize, that maximum rate regulation is one of the most important shipper and railroad concerns. It is an extraordinarily complex issue with which, as to coal, the I.C.C. has been grappling for several years in the rulemaking proceeding Ex Parte No. 347. There are no simple answers to be had at the stroke of a legislative pen. There are ways, however, to reach solutions. Over the last year, for example, a number of negotiations have been launched to address other legitimate shipper concerns about implementation of the Staggers Act. Settlements have been reached between the AAR and broadly based shipper organizations, such as the National Industrial Transportation League, and are now before the Commission for approval. Responsible shipper organizations have recognized that adequate relief can be found in good-faith negotiation with the railroads, without the need to tamper with the Staggers Act or to return to the days of stifling regulation. These shippers have learned that a sick railroad industry serves no public or private interest in the long term. The wiser course for the Congress is to allow the administrative process to work out the problems inherent in the transition from total to partial regulation of the railroad industry.

Finally, the facts show no basis for discarding the rationale of Staggers and overlaying the entire regulatory process with the draconian approach of S. 447. By any measure, there is no evidence of an abuse of the pricing freedoms provided in Staggers that might warrant such action.

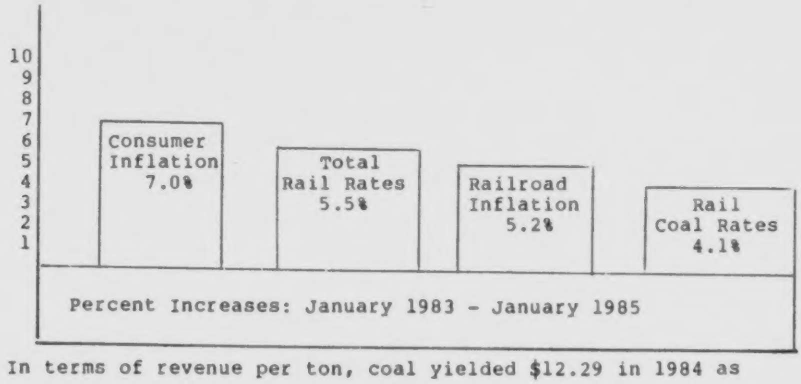
Let us look for example, at coal rates. According to the Coal Rate Index published by the U.S. Department of Labor's Bureau of Labor Statistics (BLS), railroad coal rates increased by 27.8 percent from October 1, 1980 (the date of enactment of Staggers) through January, 1985. Because the BLS Index is based on a market basket of shipments from a 1976 traffic sample, it fails to include a representative sample of contract rates (generally lower than tariff rates) and, to this extent, overstates the increase in railroad coal rates. Even so, the 27.8 percent increase only slightly exceeds the 25.7 percent increase in railroad rates for all commodities, the 24.4 percent increase in railroad inflation and the 23.6 percent increase in consumer inflation -- all between October 1, 1980 and January, 1985. The reported increase in railroad coal rates equates to an annual average increase of 5.9 percent since the Staggers Act.

This comparison is even more impressive when one considers that some of the rate increases implemented during 1981 were granted by the I.C. C. in 1980 and were premised upon historical costs incurred by the railroads prior to enactment of the Staggers Act. Furthermore, with the Staggers Act only recently implemented, few contract rates had yet gone into effect by 1981. Since that time contracts between railroads and shippers have become so popular that over 20,000 had been signed as of the beginning of 1985.

Allowing slightly more than a year for post-Staggers regulatory, marketing and pricing adjustments, the chart below shows that over the past three years, railroad coal rates have increased in total by only 6.6 percent, as compared with 10.8 percent in consumer inflation, 8.1 percent in railroad inflation and 7.0 percent in total railroad rates.



The record is better in the past two years: railroad coal rates increased by only 4.1 percent, compared with increases of 7.0 percent in consumer inflation, 5.5 percent in total railroad rates and 5.2 percent in railroad inflation.



In terms of revenue per ton, coal yielded $12.29 in 1984 as compared with $20.88 for all other traffic. In revenue per ton-mile, coal ranks dead last among the major commodity groups. While providing 22 percent of rail revenue, coal constituted 38 percent of the traffic (load on the system).

These facts show quite conclusively that market forces do indeed constrain rail rates. Further evidence is provided by the very limited use made by the railroads of their authority under Staggers to raise rates as much as 6 percent per year (reduced to 4 percent beginning October, 1983) over the inflation rate without suspension or investigation by the I.C.C. Increases actually taken under that authority amounted to .46 percent in 1981, 1.41 percent in 1982 and 0 percent in 1983. Given their inadequate revenues, had the market place permitted greater increases the railroads could very reasonably have taken them -- but the fact is they could not.

If we examine the other commodities covered by S. 447, we find comparable railroad pricing behavior. In the four year period from October 1980 through October 1984, the rate increases in constant dollars (adjusted for inflation) were:

Wood and Lumber Products	5.0%
Coal	2.6%
Ore	2.1%
Farm Products	1.7%
Chemical Products	0.6%
TOFC/COFC	-6.3%

Since it is principally the coal and utility interests which allege that rail rates have "skyrocketed", let's look at a few comparisons. Between 1972 and 1983, rail coal rates actually declined by 1.0 percent in constant dollars. They failed to keep pace with inflation. In that same period, the mine-mouth price of coal increased by 19.8 percent in constant dollars -- well ahead of inflation.

If rail coal rates are measured in cents/ton mile, a measurement which takes account of the fact that the average length of haul increased 66 percent between 1972 and 1983, we find that the rates decreased by 40 percent in constant dollars.

It is not rail coal rates that are driving up the price of electricity. Compared with the 6.6 percent increase in railroad coal rates over the past three years as shown above, the price of electricity increased by 20.8 percent through the third quarter 1984. Quite obviously, the significant increase in the price of electricity has been caused by other factors.

The supporters of S. 447 assert that the bill is necessary to correct abuses of market power that have occurred under Staggers. I submit there is no evidence whatsoever of any systemic abuse of market power in the pricing of rail service. And that is not just my conclusion. In a report last year to the Department of Energy, ICF Incorporated, a Washington consulting firm, stated:

> "Railroad ratemaking gained considerable flexibility under the 4-R Act of 1976 and gained momentum with the passage of the Staggers Rail Act in 1980. As the railroads have moved further into a deregulated environment, there have been increasing opportunities to observe railroads pricing behavior relative to the conceptual arguments presented earlier.
>
> Although many rail movements have shown substantial changes (both up and down), there is little evidence to suggest that deregulation is leading to widespread increases in rail rates above the underlying costs."

I should be pleased to answer any questions you may have.

APPENDIX

The Need For Differential Pricing of Railroad Services

Differential pricing is the pricing of each service in relation to the demand for that service. Such pricing is economically beneficial because it lowers the price of rail transportation for all shippers by encouraging the purchase of more service by shippers with a low demand for rail service. The ability to price differentially is essential to the railroads because they face strong competition for most of their traffic. Because of that competition, the revenues derived from the traffic are often not sufficient to cover both the variable and fixed costs attributable to the movement. Variable costs are costs (such as fuel) which would not be incurred except for the fact of the movement of particular traffic. Fixed costs are costs (such as roadbed) that exist independent of the movement of particular traffic. The variable costs plus an allocated share of fixed costs constitute the "fully allocated" costs of the movement (which costs include the cost of capital). Because the fixed costs are being incurred whether or not particular traffic moves, anytime the revenues from a traffic movement are sufficient to cover variable costs and make some contribution to fixed costs the traffic is desirable. The higher the degree of competition for traffic, the lower the revenue in excess of variable cost (and, hence, the lower the contribution of that traffic to fixed costs). The differential pricing of rail service is, in effect, the quantification of that inverse relationship.

The achievement of revenue adequacy for a railroad, or any other business, requires that over the long run it recover its full costs -- variable and fixed. Given the inability of railroads to recover their full costs from unregulated competitive traffic, the objective of a maximum ratemaking standard must be to regulate the rates on non-competitive traffic in a manner that is fair to the shipper who is dependent on rail service but still allow the carrier the opportunity to cover its full costs.

Differential pricing is not unfair to any shipper. Those shippers who are truly dependent on rail services -- the so-called "captive" shippers -- must ultimately be responsible for covering the full costs of the rail service they say they need. The argument advanced by some "captive" shippers that, because of differential pricing, their traffic subsidizes the competitive traffic is simply not true. To the contrary, to the extent competitive traffic makes any contribution to a railroad's fixed costs, that traffic is benefitting the "captive" shipper by reducing the amount of fixed costs that must be covered by rates on captive traffic.

Nor is differential pricing in the railroad industry something new. It has existed since the dawn of the railroad industry and has been long accepted as a necessity by the Interstate Commerce Commission. The rail transportation policy enunciated in section 101 of the Staggers Act is to allow competition "and the demand for services" to establish reasonable rates. The need for differential pricing was also implicitly recognized in the report of the Committee on Conference which observed that "All shippers as well as the carrier are better off if traffic which makes a contribution moves than if it does not, because the carrier is made financially stronger and need not rely as much on revenue from other shippers." (Report No. 96-1430 at 90)

ASSOCIATION
OF AMERICAN
RAILROADS

William H. Dempsey
President

June 12, 1985

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I refer to your letter of May 2 forwarding for my response 19 questions posed by Senator DeConcini following the Committee's hearing on S. 447. I regret the delay in submitting this response but, as indicated by its length, the questions were deserving of and received full and careful consideration.

If I can provide any further information to the Committee, I shall be happy to do so.

Sincerely,

WH Dempsey

enc.

1920 L Street, N.W., Washington, D.C. 20036 (202) 835-9126

Questions Asked by
Senator DeConcini
and
Mr. Dempsey's Responses

Question 1. Mr. Dempsey, if S. 447 were modified so that there was no question that the district courts would not impose rate reasonableness standards upon the railroads duplicating those jurisdictional powers granted to the Interstate Commerce Commission, would you then be in a position to support the bill? If not, what further changes would you see as necessary in order to remove any duplication between the powers granted to the Interstate Commerce Commission under the Interstate Commerce Act and those that would be granted to the district courts under this bill?

Answer. S. 447 is hopelessly at odds with the regulatory structure set out in the Interstate Commerce Act. For that reason, the two schemes cannot be harmonized.

First, the Interstate Commerce Act, as reflected in the Staggers Act provisions, and S. 447 begin from different premises. In respect of "captive shippers," Staggers balances the need to protect shippers with the need for railroads to earn sufficient revenues to attract private capital. S. 447 begins with the presumption that the "captive shipper" -- as uniquely defined in the proposal -- is the victim of an unlawful monopoly in need of special protective sanctions without regard to the financial viability of the railroads.

Seeking to serve different objectives, the remedial provisions are in conflict. For example, S. 447 would, if the grant of trackage rights did not yield the desired effect, prevent the owner railroad from seeking more than a pro rata share of its full costs from the "captive shipper." As noted in my testimony, most rail traffic is highly competitive and moves at rates below fully allocated costs (i.e., fixed plus variable costs). That traffic benefits the "captive shipper" by making a contribution to fixed costs which the captive would otherwise have to make. Charging the competitive traffic its pro rata share of those fixed costs would only cause its diversion to competing carriers. Thus, the formula of S. 447 will force the railroad to set rates so high that its most competitively vulnerable traffic will desert it, or to set them so low that its full cost will not be recovered.*/

Staggers, on the other hand, does provide for an inquiry on rate reasonableness and the establishment of maximum rates where a railroad is "market dominant," that is, where there is an absence of "effective competition" -- and in determining the presence or absence of competition, all forms of competition are considered. However, the zone of inquiry begins with the 180 percent revenue/variable cost test -- without respect to any proration among shippers -- and then only if the facts reveal a true market dominance. In determining the reasonableness of rates where market dominance is found, the needs of the carrier for revenues necessary to maintain a viable railroad are taken into account. This is in marked contrast to S. 447 which not only presumes market dominance (captivity) wherever a shipper is served by only one rail carrier, but totally ignores the need for a railroad rate structure that provides revenues sufficient to maintain the system over the long run.

So long as S. 447 provides an avenue of judicial attack against a rate that would be deemed reasonable under the Interstate Commerce Act, its unnecessary jurisdictional conflict remains inevitable. And even were the entire Interstate Commerce Act to be repealed by S. 447, the special provisions regarding the shipment of bulk commodities would still be unworkable because they ignore the true state of competition and the need to differentially price rail services.

Question 2. Isn't it a fact that while the Interstate Commerce Act technically may provide certain remedies for some anticompetitive railroad acts, it has no effective sanctions that would discourage railroads from engaging in these acts? Isn't it also a fact that even if a railroad is found to have engaged in anticompetitive conduct in violation of the Interstate Commerce Act, there are no damages possible that would make a shipper or a competing carrier whole?

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*/ It is to be noted that the truly captive shipper loses in both instances. In the first instance it has to bear the share of fixed costs previously allocated to competitive traffic. In the second instance, it will ultimately lose the rail service it is, by definition, totally dependent upon.

Answer. No. The Interstate Commerce Act contains a comprehensive remedial scheme that provides effective sanctions including compensatory damages for violations of that Act. Civil and criminal penalties are provided for violations of the substantive provisions of the Act and of ICC orders issued pursuant to it. See, e.g., 49 U.S.C. §§11901 and 11914. The ICC may in some circumstances order compliance with provisions of the Act and bring a civil action against a railroad that violates such orders. See 49 U.S.C. §11702. Finally, persons injured as a result of any violation of the Act by a railroad are expressly authorized to recover damages under that Act. See 49 U.S.C. §11705.

Question 3. At page three of your testimony you state that under S. 447 if a shipper or another rail carrier seeks to use a sole facility, the railroad owner has no choice but to open the facilities for a rental to be set by "vague and uncertain standards." If the bill were modified so as to make it clear that the standard would be the same standard that the district courts would use in essential facility or bottleneck monopoly cases, would you then still consider these standards to be vague and uncertain?

Answer. Yes. The essential facility or bottleneck monopoly cases have not set any compensation standard at all, "vague and uncertain" or otherwise.

The essential facilities doctrine provides that, in certain circumstances, a monopolist may not deny access to his facilites to his competitors because, to do so, can extend monopoly power from one stage of production to another, and from one market into another. MCI Communications Corp. v. ATT&T, 708 F.2d 1081, 1132 (7th Cir. 1983). Thus, within the limits of feasibility and the practical difficulties of duplicating a facility, the antitrust laws have in certain circumstances imposed on firms controlling an essential facility the obligation to make the facility available to competitors on non-discriminatory terms. Id.

While the concept of non-discrimination is meaningful in the situation where the monopolist denies access to one competitor but not another, its application is uncertain where access has been denied to all. Assuming a circumstance where the essential facilities doctrine applied, the cases have not addressed the essentially regulatory concern of what price the monopolist should charge. In the Supreme Court's Otter Tail decision, for example, the Court left this question open to the regulatory process under the auspices of the Federal Power Commission, and the matter was never at issue in the MCI case. Thus, providing in the bill that the district courts would use the same standard as used in essential facilities would not be to establish standards, but rather to leave the district courts in unchartered waters, undertaking without the benefit of regulatory expertise an essentially regulatory task. The inability of district courts to function effectively as rate setting bodies was one of the principal factors motivating the Congress to establish regulatory agencies.

I would like to offer some further observations on the matter of trackage rights. Section 11103 of the Interstate Commerce Act authorizes the ICC to require a rail carrier to permit use by another rail carrier of its terminal facilities, including main-line tracks for a reasonable distance outside of a terminal. That is as far as existing law goes in compelling trackage rights and, for two fundamental reasons, that is as far as it should go.

First, the incentives and ability of railroads to construct or maintain facilities would be significantly undermined by a policy that permitted rivals to force the sale of rights to utilize them. Second, railroads have strong incentives to voluntarily permit others to utilize their facilities, at mutually advantageous terms, wherever it is the case that utilization would be efficient.

Since enactment of the Staggers Act the railroads have invested more than $60 billion in maintaining and improving their track and roadbed. It is a basic economic precept that there can be no commercial investment without property rights. Absent the ability to earn the fruits derived from investment, there is no incentive to invest, only the certainty of financial losses. Moreover, without the property rights over assets that permit the investor to earn returns, there can be no competition in markets that require investment for services to be supplied.

This is the fundamental reasoning that underlies our systems of patent and copyright protection. Without protection of property rights over the achievements of research and development and authorship, too little innovation and creation would be forthcoming. This is also the rationale behind the inability of a fast food vendor to utilize the legal system to force an existing successful competitor to share his site with the newcomer. If competitors could be forced to share their assets with their rivals, firms would have little incentive and financial ability to undertake investment in the first place.

The danger to investment incentives is especially great in the railroad industry due to the nature of railroad costs. Railroads have very high investment requirements to create the capacity needed to provide rail service. A large portion of these costs are fixed -- that is, they do not vary with the amount of rail service provided. If a significant portion of a railroad's existing or anticipated traffic is diverted, its substantial investment in fixed capacity nevertheless remains. And if it is unable to cover the costs of that capacity, investors will not supply new capital to repair and, eventually, replace the railroad's facilities.

Another aspect of a railroad's cost structure is also important here. A high portion of a railroad's fixed costs are incurred on behalf of more than one service. That is, they are common costs. This means that the uncompensated diversion of traffic which makes or could make a substantial contribution to the railroad's fixed and common costs affects not only the railroad's ability to provide the same service in the future, but will also lead to deterioration in the railroad's ability to provide its other services which share the same facilities -- unless those other services are in a position to increase substantially their contribution to the railroad's costs.

From the standpoint of the public interest, these effects are particularly baneful where the railroad's facilities constitute the most economically efficient means of providing a particular service or set of services. Where those facilities are uncongested, the greater the use of the railroad's fixed plant, the lower the average cost of service. This means that the most efficient facilities can provide the most service at the lowest cost to the involved shippers, thereby making the most beneficial use of the nation's transportation resources.

Thus, a policy that entails forcing a railroad to permit its rivals to utilize its facilities would pose a serious threat to the efficiency with which railroad assets are employed. The financial terms set for a forced sale of utilization rights are likely to entail inefficiently small remuneration, because legal coercion would have been unnecessary if the terms were genuinely compensatory. Then the railroad obtaining access would achieve competitive advantages over the other carrier that were artificial and unrelated to true efficiency advantages. The inevitable result would be inefficient diversion of traffic volume and unnecessarily high industry costs for the transportation services provided. Even more serious in its long run consequences for the national rail network and the shippers who rely on it is the threat forced sales of utilization rights would pose to railroad investment. Investors would be understandably leery about undertaking new railroad investments in the face of a policy permitting the revenues expected from the investments to be siphoned off by another rail carrier through the forced sale of their property rights below market prices.

Not only do forced sales of rights to utilize railroad facilities entail significant social costs and pose a serious threat to the long-term health of the railroad industry, they generally fail to generate any countervailing benefits to society. The essential reason is that any potential social benefits of shared utilization of railroad facilities will generally be realized by voluntary arrangements between rail carriers, provided that the rail carriers have secure property rights to their facilities and have the right to price the services of their facilities independently. Under these circumstances, if the rail carrier seeking utilization of another's facilities would experience benefits that exceeded the costs that would be imposed on the owner, then the two parties would have strong incentives to agree on mutually advantageous terms. The financial arrangements would compensate the owner for the costs (including lost revenues) caused by the other rail carrier's utilization of its facilities, while, at the same time, not exceed the benefits derived by that railroad from its access to the facilities. Obversely, under these same circumstances, mutually advantageous terms could not be found if the benefits from a carrier's utilization of another's facilities fell short of the associated costs.

In this fashion, the outcome of freely competitive bargaining between an owner of railroad facilities and another railroad seeking their utilization can be expected to coincide with the arrangement that is maximally efficient. Moreover, it is the freely competitive bargaining process that best assures incentives for efficient investments in facilities to be undertaken. When investors recognize that they can augment the revenues earned from their own operations with revenues derived from voluntary arrangements with other rail carriers, their investment decisions will weigh the total net benefits available from new facilities against the associated total costs of constructing them. These socially efficient outcomes contrast sharply with the stultification of investment that is the likely result of forced sales of utilization rights.

While advocated by some shippers, the forced sale of trackage rights would be contrary to the long-run interests of rail shippers as a whole. While some shippers might enjoy temporary benefits from rail rates made possible only by the forced sale of utilization rights at noncompensatory terms, those benefits would self-destruct as the facilities in question were left to deteriorate and ultimately to be retired because of the inadequate returns they brought to their under-compensated owners. Moreover, the temporary benefits conferred on some shippers by the forced sale of utilization rights could exact costs at least as great from those other shippers who would be called upon to make up for the contribution lost from the directly affected traffic or to suffer from a deterioration in rail service.

Question 4. At pages three and four of your statement you suggest that the current bill is unnecessary because, in fact, railroads face substantial competiton for a large portion of their traffic. Let us examine a situation where competition does, in fact, exist and rail rates are, therefore, at the competitive level. In such a situation, what possible reason would a shipper have for seeking the operative provisions of the bill so as to provide a duplicate rail service that could not possibly lower his transportation charges? Also, in such a situation, what possible incentive would a competing rail carrier have to seek entry into a market when there is already a competitive rate level? It seems to me, Mr. Dempsey, that the only time this bill's provision with respect to competitive access would come into play would be in those circumstances where, in fact, the competition was not adequate to ensure a competitive rate but, in fact, the railroad had sufficient market power so that it was charging supra competitive rates. Would you agree?

Answer. I do not agree that S. 447 would only be resorted to when there was an absence of effective competition or that, when rates are at a "competitive level", a shipper would have no incentive to trigger the provisions of S. 447. Matters do not fall so easily into black or white boxes. Rail rates do vary in accordance with the demand for rail services. At one end of the rate spectrum might be a shipper totally dependent upon rail transportation and at the other a shipper who can ship as easily by truck as by rail. Within the zone of competition, S. 447 could give shippers substantial bargaining leverage in driving down rates which were already competitive. S. 447 would be an invitation to shippers to attempt to gain through the threat of litigation advantages which are not available under the regulatory framework created by the Congress.

To begin with, S. 447 is practically risk-free for a shipper seeking to gain an advantage. A monopoly is presumed in the bill, merely by virtue of there being only one rail owner; since monopolistic conduct need not be proven, the shipper risks little in beginning the process. On the other hand, once the process is begun the rail owner is faced with a difficult and expensive task -- negotiating or litigating trackage rights with another carrier and, if that fails to induce competition -- defending a complicated court proceeding regarding the determination and proration of a "fair return" on its "prudent investment" in the rail facility. The shipper, meanwhile, may at any time be able to divert his traffic to trucks or barges, since S. 447 does not take intermodal competition into account. The threat of diversion and the prospect of being put through a costly process places the railroad in a much weaker bargaining position with the shipper even when the existing rate already reflects competition.

The shipper may have other incentives. It might wish to use S. 447 to force a connection with a water carrier pursuant to the proposed section 9(c) of the Sherman Act. It might seek to utilize the threat of activating a process under S. 447 in order to gain an advantage over the railroad in respect of other traffic. Finally, the shipper might wish to ascertain what the maximum rate for the traffic might be under proposed section 9(a)(3).

A competing rail carrier might also seek to enter the rail owner's market under a similar "nothing ventured, nothing gained" theory. Litigation always carrying some uncertainty, the competing rail carrier might hope that the vague terminology regarding "generally accepted principles regarding just and reasonable rental of track" might be construed as permitting it to pay on a compensation standard less than the capitalized value of the earnings of the rail owner attributable to the line. This is not totally unlikely, since the courts, unlike the ICC under Staggers, have no mandate to protect the railroads' opportunity to secure long-term financial viability. If the gambit fails, there is no requirement that the competing rail carrier avail itself of the trackage rights sought. There can only be one loser: the rail owner.

Similarly, the competing rail carrier might use the processes of S. 447 as leverage for concessions or in retaliation against actions taken by the rail owner in respect of other rail traffic.

Last, both the shipper and the competing rail carrier might find a bargaining chip in the in terrorem aspects of S. 447. As noted in my testimony, the standards of S. 447 are untested. The prospect of paying treble damage by guessing wrong on a new law materially changes the odds in negotiating rates or terms of trackage rights.

Question 5. On page four of your testimony you state that railroads are already subject to the antitrust laws if they engage in "predatory or anticompetitive pricing or practices." Could you give me a single example of where a shipper is able to prevent a railroad from engaging in any predatory or anticompetitive pricing practice by an injunction or by treble damage remedy in the event of substantial damages to that shipper? It is a fact, is it not, that under the Keogh case a shipper simply cannot recover treble damages for anticompetitive rail actions and that under §16 of the Clayton Act, a shipper simply cannot obtain injuctive relief for anticompetitive railroad practices?

Answer. The general applicability of the antitrust laws to the railroad industry is discussed in my answer to your Question 12. In answer to this question, however, let me emphasize that the sentence that you quote from page 4 of my testimony is correct. "Railroads are already subject to the antitrust laws if they engage in predatory or anticompetitive pricing or practices."

The Interstate Commerce Act regulates pricing somewhat differently than it does practices with respect to other matters. The Keogh case, which you refer to and which I discuss in more detail in my answer to Question 12, dealt only with pricing -- and specifically rates contained in tariffs on file with the Interstate Commerce Commission. Except where express antitrust immunity has been afforded by Congress or where antitrust immunity arises by virtue of the regulatory authority of the ICC, predatory or anticompetitive practices with respect to other matters remain subject to the antitrust laws.

The antitrust laws also apply in certain circumstances where railroads are alleged to have engaged collectively in "predatory or anticompetitive pricing." As discussed in my answer to Question 12, by virtue of an amendment to the Interstate Commerce Act adopted in 1948 (the Reed-Bulwinkle Act), railroads can obtain express antitrust immunity for certain collective ratemaking taken pursuant to agreements approved by the ICC. As I noted at pages 4-5 of my testimony, however, the protection afforded to the railroad industry by this provision has been severely limited by the Staggers Act and subsequent ICC decisions which withdraw immunity for collective rate action in many situations where it previously applied. Collective rate action by railroads outside the protection of an approved agreement could subject the railroads to an antitrust suit and to an injunction from an antitrust court prohibiting such collective action -- whether that rate action was predatory, anticompetitive, or otherwise -- if the antitrust laws are violated. See, Georgia v. Pennsylvania R. Co., 324 U.S. 939 (1945).

Moreover, the United States Court of Appeals for the District of Columbia Circuit has suggested that the express antitrust immunity afforded by the Reed-Bulwinkle Act to collective rate action under an ICC-approved agreement can be lost if that rate action can be shown to be "predatory or anticompetitive" -- or, in the court's words, if it is "part of an effort by [r]ailroads in combination or conspiracy" to eliminate competition. See, Atchison, Topeka & S.F. Ry. Co. v.Aircoach Transp. Ass'n, 253 F.2d 877, 887 (D.C. Cir. 1958). Although this principle seems inconsistent with both the language of the Reed-Bulwinkle Act and its legislative history, it has been applied by several lower court decisions, although primarily in the District of Columbia.

It is not true that under Keogh "a shipper simply cannot recover treble damages for anticompetitive rail actions." There are a great many different kinds of "actions" that are subject to the antitrust laws, to which Keogh has no application; Keogh relates only to rates. And with respect to rates, while Keogh would deprive a court of the power to award treble damages for charging allegedly excessive rates, the ICC has ample power to award fully compenatory remedies to shippers and competitors who claim injury from rates that violate the substantive provisions of the Interstate Commerce Act.

Similarly, it is not true that "under §16 of the Clayton Act a shipper simply cannot obtain injunctive relief for anticompetitive railroad practices." Again, a great many different kinds of anticompetitive practices are not subject to §16, which applies only to matters "subject to the regulation, supervision or other jurisdiction" of the ICC. And as to those matters the ICC has, as I have said, adequate and effective remedial powers and sanctions.

Question 6. At page six of your statement you suggest that the Interstate Commerce Commission has jurisdiction to rule upon rail rates only when those rates exceed 180% of variable cost. The purpose of S. 447 is to eliminate the necessity for ICC involvement by substituting competition and normal marketplace forces for the regulatory process. Would you agree with the overall objective of the bill and would you state that allowing competition and normal market forces to regulate the railroad industry is by far preferable to ICC regulation?

Answer. I cannot agree with the overall objective of S. 447 because it does not purport to subject the railroads to the antitrust laws in lieu of the existing regulatory regime. To the contrary, it would set up special antitrust remedies -- not applicable to any other industry -- in addition to the existing regulatory regime. Given a true choice, I would certainly prefer to see railroads governed by the normal rules of the marketplace and treated just as any other business, rather than by a special regulatory system. In that regard, the Staggers Act comes much closer to that objective than would S. 447 in two ways.

First, S. 447 does not eliminate any of the necessity for ICC involvement. Instead, it adds a totally new judicial regulatory scheme. The grant of trackage rights would be governed by a special standard to be tested by the court system. Bulk commodities, as uniquely defined, would thus be subject to two types of maximum rate criteria, the test under Staggers, as administered by the ICC, and the test under S. 447, as administered by the courts. Differential pricing, permitted under the former, would presumably be outlawed under the latter.

Secondly, the existing Staggers test for maximum rates permits the ICC to take marketplace factors into account. Product, geographic and intermodal competition may be considered in determining market dominance and the presence of effective competition. S. 447, on the other hand, looks only at rail competition. No bill can claim compatibility with marketplace conditions which does not recognize the modal competition which characterizes that marketplace.

Questions 7 and 9. You spend a good deal of time in your statement talking about the concept of differential pricing and its place in the railroad industry. Would you agree with me that differential pricing has absolutely no application in a free market situation and the only

> reason for its existence is because of regulatory restraints? If you disagree with that statement, would you please explain how differential pricing operates in the unregulated economy and in the marketplace generally?
>
> Further, on the issue of differential pricing, you state that since certain commodities are carried at less than their full cost, other commodities must bear a higher than full cost burden in order to make the entire enterprise profitable. How is it that motor carriers and barge lines and airlines exist in a highly competitive market without the ability to price on a monopoly basis and do so without the concept of differential pricing? Furthermore, it seems to me that if the railroad involved seeks to carry products at less than their full costs that that is the railroad's own choice and it should not be allowed to rely upon that choice in order to price at a monopoly level on the other shipments. Wouldn't you agree? It also seems to me, Mr. Dempsey, that the entire concept of differential pricing is in fact a word game. Any enterprise produces a certain level of output over which is spread its full cost. Pricing must be at a level that recovers this full cost if the enterprise is to succeed. Any additional output may then be priced at its variable or marginal cost plus some element of return which then goes to lower the overall burden being carried by the then existing full cost output. Your concept of differential pricing seems to stand this concept on its head. You suggest that the first units of output are priced at below their full cost. Therefore, it is necessary, you say, to price at the monopoly level in order to make the whole enterprise profitable. If this is not nonsense, I would like you to explain to me why it is not nonsense.

Answers. Because both Questions 7 and 9 deal with differential pricing, I am combining them to avoid repetition in my response. As to Question 7, I do not agree with the statement that "differential pricing has absolutely no application in a free market situation and the only reason for its existence is because of regulatory restraints." Nor do I agree with the suggestion in Question 9 that differential prices are monopoly prices. I will deal with that matter first.

As a predicate to my answers to these questions let me attempt to clarify a sometimes definitional problem. I assume the term "full cost" is used to mean "fully allocated costs". "Fully allocated costs" is a term sometimes used by the Commission which includes the variable costs of a particular movement plus an arbitrary (usually pro rata) allocation of total fixed and common costs. By definition, these "full costs" represent neither the total costs of a railroad's entire set of services nor the economic cost of any particular movement. Accordingly, for the purposes of assessing the economic and competitive significance of a railroad's prices, the concept of "full cost" or "fully allocated costs" has no meaning except as an arbitrary benchmark used by some critics of differential pricing as a basis for their claims that some differential prices exceed an economic level.

Differential prices may be set at levels below or above the level of "fully allocated costs." In the aggregate, they are intended to recover no more than the total costs of the railroad service. By definition, differential prices are set according to demand as well as to marginal or incremental costs. Differential prices may yield total revenues that fall short of the railroad's total costs or total revenues that just recover total costs. So long as differential prices do not produce revenues which exceed the railroad's total costs, they cannot properly be termed monopoly prices. Further, differential prices may be set by firms involved in fierce competition with other firms who may or may not themselves set differential prices, and on this score, too, there is no proper identity between differential prices and monopoly prices. Moreover, and most important, differential prices help to recover fixed and common costs in the manner that most benefits consumers as a group, while the term "monopoly prices" connotes prices that are harmful to consumers. Thus, the distinction is one of substance vital to consumers' interests, rather than one of mere semantics, and, for this reason, it may be worthwhile to spell out more fully the differences.

The hallmark of monopoly prices, as the term is usually employed by economists and antitrust authorities, is that they earn monopoly profits -- the excess of revenues over the funds needed to defray the costs of efficient operation and the costs of needed capital. Monopoly prices may be differentiated, as are differential prices, or they may be uniform depending on circumstances. In either case, they are too high because lower prices would be sufficient to cover operating costs and to provide the returns to capital needed to attract investment funds. Because they are unnecessarily high, monopoly prices enrich the firm that sets them at the expense of the consumers that pay them. However, the real social damage from monopoly prices goes well beyond the coerced transfer of wealth from consumers to the firm. Monopoly prices repress the output of the firm and the quantities of goods and services enjoyed by consumers. Thus, they cause a diminution of productive activity in the economy and a drop in the general standard of living.

While all this may be obvious, once stated, it should be equally obvious that differential pricing of railroad services, under the Staggers Act, is as good as monopoly pricing is generally bad. Differential pricing of rail services under the Staggers Act does not now, and will not be permitted to, earn revenues for the railroads beyond those deemed to be adequate for the recovery of efficient costs. Thus, totally unlike monopoly prices, differential prices do not force consumers of rail services to pay too much or to transfer wealth to railroad firms. Instead, over time, they may afford the railroads the opportunity to be successful in covering their costs, for the first time in many years, and in making the capital commitments for continued high quality services that financial health will make possible.

Moreover, totally unlike monopoly prices, differential prices do not repress the output of rail services or the rail transportation enjoyed by shippers. Instead, to the contrary, differential prices are designed to stimulate the utilization of the rail network and the provision of rail services to shippers. By their responsiveness to market demand, differential prices maximize the volume of service and permit the movement of all traffic whose benefits from rail service exceeds the costs that it causes. In this manner, differential prices provide more benefits to the totality of shippers, both "captives" with their high demand for rail service and those with other, albeit less efficient, transportation options. The result is better transportation nationally, more productive output from the economy, and a higher standard of living for the ultimate consumers of the goods transported.

A simple example can most clearly demonstrate the beneficial workings of differential pricing and answer some of the portions of Question 9. Consider a railroad with total unattributable fixed and common costs of $360 million, and two types of potential traffic, A and B. Service A would, if necessary, be able to pay $300 million above its attributable costs, while service B would be able to pay only $100 million above its attributable costs. These figures reflect the value of rail service to the shippers involved. Suppose that traffic A and B entail equal quantities of ton-miles and tons of shipments. Then, if the railroad were forbidden to practice differential pricing, it could only set a uniform price that would seek from each service $180 million above attributable costs, in the hope of recovering the total figure of $360 million. However, service B could not pay this uniform price, because it exceeds the value of rail service to its shippers.

By pricing service B out of the market, the railroad would face a shrunken traffic base and would have to attempt to recover its costs entirely from service A with a price of $360 million above attributable costs. However, since service A can pay at most $300 million, the railroad would be condemned to revenue inadequacy, and the shippers of the high value service A would be condemned to paying the most they could for rail service that would deteriorate over time and eventually disappear due to the excess of costs over revenues.

In contrast, these problems would be solved for all parties by differential prices. The railroad could charge demand-based rates that would raise contribution of $270 million above attributable costs from service A and $90 million above attributable costs from service B. The market determined differential prices allow both traffic A and B to move, and permit total costs, both attributable costs and unattributable fixed and common costs to be recovered. As a result, shippers A receive net benefits of $30 million ($300 - $270), while shippers B receive net benefits of $10 million ($100 - $90) from service that need not deteriorate nor be discontinued because its total costs are covered by revenues. Here, differential prices permit more traffic to move, yield lower prices for the high value traffic B, and support a financially healthy and more fully utilized rail system.

Question 9 asks "if the railroad involved seeks to carry products at less than their full costs that is the railroad's own choice and it should not be allowed to rely upon that choice in order to price at a monopoly level on the other shipments. Wouldn't you agree?" I would not agree because, as the example makes clear, the decision to price the low demand service A at a level below average, but above attributable cost, permits that traffic to move and to make a contribution to fixed and common costs that decreases the portion that must be recovered from the high demand traffic. Absent differential pricing, and absent low value traffic, high demand traffic would inevitably face higher prices and lower quality, or disappearing service. Moreover, as can be seen from the example, the high demand traffic B is faced with no monopoly prices -- neither with nor without the presence of the low demand traffic and the differential prices that permit it to move.

Question 9 also asks for an explanation, it seems, of the order in which differential prices are set. Is it the low demand traffic that is priced first with the prices of the high demand traffic following, or vice versa? In a real sense, there is no such order. Prices are set simultaneously, or with no purposeful order as contract negotiations and regulatory deliberations come to their individual conclusions. In the example above, the differential prices are set in no order -- they are both set at the relationship to willingness to pay that is sufficient to generate adequate total revenues. On the other hand, under the Staggers Act, an analysis of revenue needs -- if not the actual setting of rates -- does follow a natural order. Since there is no direct regulation of the prices of services provided under contract and of services that are not market dominant, the revenues needed from regulated services to recover total costs are calculated as an arithmetic residual. This analytic method works to the benefit of the shippers whose prices are directly regulated, because the railroads have every incentive to obtain the most net revenues they can from the traffic under contract and from the traffic that is not market dominant. Clearly, the ability to set differential prices on all these categories of traffic is a key to minimizing the revenues that are needed for cost recovery from any one group of shippers.

I will now return to Question 7 and the first portion of Question 9 concerning the use of differential pricing outside the railroad industry and outside the domain of regulation. Since differential prices are the best way to recover fixed and common costs in terms of benefits to consumers and in terms of the utilization of resources, it should come as no surprise that their use is not limited to the sphere of regulation.

To see differential pricing at work, one need look no further than the passenger airline industry. On most flights, passengers sitting in identical seats can be found to have paid widely different fares under discounts subject to seemingly arbitrary restrictions. The restrictions serve to separate groups of potential passengers who, on average, have differing levels of willingness to pay, but who impose equal costs on the airline. For example, low round-trip fares that apply to passengers staying at their destination over the weekend are expected to attract pleasure travelers, but are not needed to attract business travelers who, on average, are willing to pay the higher unrestricted fares. By pricing differentially in this fashion, airlines are able to cover the substantial fixed costs of each flight, and to support a large number of conveniently scheduled flights. Of course, today, airlines are both extremely competitive and unregulated in their pricing.

Highly competitive supermarkets practice differential pricing through the institution of coupons for discounts and double discounts of items identical to those bought at higher prices by customers without the inclination to shop for bargains and collect the coupons. The film industry sets differential prices for first-run showings, second-run showings, cable TV rights, video cassette rentals, and broadcast TV rights. The difference between prices for books in hardcover and softcover reflect differences in demand more than differences in costs of binding. Movie houses give "golden age" discounts to patrons on social security in order to fill seats rather than to altruistically support the retired. Volume discounts at package stores sell more beer by the case at compensatory prices. Journals set subscription prices to libraries at double or triple the rate available to individuals for the same item. Those who say that auto manufacturers enjoy higher profit margins on big cars than on small cars are asserting that differential pricing characterizes that highly competitive industry.

In most, if not all of these examples, and in countless others limited only by the observer's experience and acuity, firms in free market situations employ differential pricing. They do so to cover their fixed and common costs, to permit the expenditure of more of these costs in order to provide more attractive goods and services, and to meet the competition they face with price structures that provide maximal benefits to their customers. While firms in free markets are motivated to employ differential prices by their desire to survive and prosper, they are at the same time promoting the public interest by improving the utilization of resources and providing consumers with more benefits. Thus, differential pricing is an inherent attribute of unregulated markets. It is only under regulation that decision-makers must consciously understand the connection between differential pricing and the public interest.

Question 8. At page eleven of your statement you seem to suggest that any application of the essential facilities doctrine where a rental is less than the capitalized value of the revenue that the property is producing or capable of producing would constitute an unlawful taking of property without due process. Are you suggesting that the decisions of the Supreme Court in the Otter Tail case and of the Seventh Circuit in the MCI case, are, in fact, unconstitutional in that regard?

Answer. As noted above, the essential facilities cases do not establish a standard by which to determine the rental that, in appropriate circumstances, a monopolist would charge a competitor. The Supreme Court explicitly left this issue to the Federal Power Commission in Otter Tail, and the Seventh Circuit never had occasion to address the issue in MCI.

Question 9. Answered with Question 7 above.

Question 10. I must say, Mr. Dempsey, I was very concerned with your statistics on coal movements. First, you seem to use different time periods when comparing increases and decreases in various costs. For example, you use the periods 1980-1984 for one purpose and then you use the period 1972-1983 for another purpose and then you use the period 1980-1985 for yet another purpose. More importantly, however, you use the period 1972-1983 and you state at page seventeen in your testimony:

> If coal rates are measured in cents/ton mile, a measurement which takes account of the fact that the average length of haul increased 66% between 1972 and 1983, we find that rates decreased by 40% in constant dollars.

When you made the comparison in rail rates, did you take into account that in 1972 a large portion of the coal transportation was for single car shipments for relatively short distances and in carrier owned equipment, thereby resulting in very high cost transportation in relative terms? Did you also take into account that in 1983 a much larger portion of the coal was moving in very long haul unit trains with the shippers supplying the equipment? It seems to me, Mr. Dempsey, in order to prove your point, you have not compared apples with apples, but rather, simply by looking at rates without relation to the costs, you have greatly skewed the numbers. Would you care to comment upon this?

Answer. In regard to your first concern about the use of different time periods "when comparing increases and decreases in various costs," three points are pertinent. First, it is not "costs" which are being compared; rather, it is railroad coal rates over time and relative to rates of other commodities being hauled by railroads. Second, the use of 1980-84 versus 1980-85 is a function of the latest available data at the time that my testimony was prepared. In either case, the trend of railroad coal rates is similar. And finally, the use of 1980-84/85 data versus 1972-83 is a matter of showing both the long-run (prior to the first energy crises) and short-run (since Staggers) trend of railroad coal rates. In retrospect, I should have used 1972-85 for the later trend analysis, but simply adopted 1972-83 because we have used that period in the past when making comparisons with other data bases where more current data were not available. Again, the trend of railroad coal rates is similar for any of the periods used -- that coal rate increases have been modest by any standard of measurement.

Your other concern is with the application of a general railroad inflation index to coal revenue per ton-mile, instead of a more specific index which measures changes in the cost of transporting coal by railroad. The problem here is that there is no inflation index for railroad coal movements, so that the railroad inflation index is used as a surrogate. The one area where railroad coal rates are viewed in relationship to costs is in the calculation of revenue-to-variable cost ratios. This calculation, undertaken by the Interstate Commerce Commission, shows that in 1982 the average revenue-to-variable cost ratio for railroad coal movements was 146 percent -- a level far below the 180 percent jurisdictional threshold. When the ICC calculates cost applicable to coal traffic, it accounts for longer hauls, heavier loadings and other efficiencies by making cost adjustments (i.e., fewer number of switches, multiple car movements, etc.) and allocating costs on a unit basis, considering tons handled and miles transported. Thus, changes in coal transportation, such as you suggest, are accounted for in the ICC's determination of revenue-cost ratios.

Question 11. At page eighteen of your statement you quote from an organization called ICF Incorporated. Could you supply a complete copy of the ICF report and if it is not otherwise indicated, please indicate who requested and paid for that report.

Answer. A copy of the ICF document to which I referred is enclosed. I erred in stating the document was prepared for the Department of Energy. It was prepared for the Environmental Protection Agency and I assume that agency paid for the report. In addition to the principal point it makes -- that there is "little evidence to suggest that deregulation is leading to widespread increases in rail rates" -- I would also call to the Committee's attention the report's discussions of competition in the rail industry and the need for differential pricing.

Question 12.	Mr. Dempsey, during the examinations during the hearing on April 23, in response to a question from Mr. Feidler of the Committee staff, you were somewhat unclear as to the current application of the antitrust laws to the railroad industry. Would you sir, for the record, give us your understanding of the remedies available to shippers and, separately, to competing carriers for railroad antitrust abuses. Would you specifically give us situations where you think the antitrust laws either through treble damage or injunctive relief, would be applicable and examples where the antitrust laws would be inapplicable?

Answer. The antitrust laws are fully applicable to the railroad industry except as to those activities where an express exemption from the antitrust laws has been provided by statute or where the regulation of those activities by an administrative agency under another statutory regime has been deemed to displace the antitrust laws in favor of exclusive regulation by that agency.

As to express antitrust exemptions, for example, the Interstate Commerce Act puts approval of consolidations, mergers, and acquisitions of control among railroads under the exclusive jurisdiction of the Interstate Commerce Commission (ICC) and expressly exempts the carrying out of such approved transactions from the antitrust laws. See 49 U.S.C. §§11341-11346. Under a provision originally enacted in 1948 as the Reed-Bulwinkle Act, the making and carrying out of certain kinds of agreements among railroads relating to rates or the joint establishment of rates is expressly exempted from the antitrust laws if the ICC has approved the agreement. 49 U.S.C. §10706. To the extent that the railroads were to act collectively with respect to rates outside the scope of an ICC-approved agreement, however, they would be subject, under the principles of Georgia v. Pennsylvania R. Co., (1945), to an antitrust action seeking an injunction barring such collective action.

As to antitrust exemptions arising by virtue of agency regulation, the ICC's jurisdiction under the Interstate Commerce Act over railroad rates contained in tariffs on file with the ICC is so extensive that antitrust actions attacking these rates and seeking antitrust damages have been barred by §16 of the Clayton Act and by the Supreme Court's decision in Keogh v. C.&N.W. Ry. Co., 260 U.S. 156 (1922). These tariff rates are subject to ICC regulation under the substantive standards of the Interstate

Commerce Act, however, and as suggested in my answer to Question 2, the Act provides a comprehensive remedial scheme for violation of those standards. This scheme includes the power of the ICC, in certain circumstances, to prescribe rates and to compel a railroad to charge only those rates. See 49 U.S.C. §10704-10705. In addition, the statute authorizes compensatory damages for violations of the substantive provisions of the Act or of an ICC order issued pursuant thereto. See 49 U.S.C. §11705. To date, cases applying Keogh have involved rates contained in tariffs on file with the ICC. It is uncertain, therefore, whether Keogh will be found to apply in a case where the rates involved are not contained in filed tariffs because the transportation is covered by contract (49 U.S.C. §10713) or has been exempted by the ICC from its jurisdiction (49 U.S.C. §10505). There also are a few lower court decisions which suggest -- erroneously, I believe -- that the Keogh doctrine is inapplicable in antitrust actions brought by a competitor rather than by a shipper.

Question 13. The Otter Tail and MCI cases set out the duties of the owner of an essential facility. Basically, this doctrine requires that competitors be able to use the essential facility on "fair" or "equal" terms. Let me give you a recent fact situation. The Southern Pacific has strictly and steadfastly refused to allow the Union Pacific access to its lines leading to a new Toyota/GM plant in California. In your opinion, has the Southern Pacific violated the essential facilities doctrine? Does this doctrine even apply to railroads? Should it?

Question 14. In the Toyota/GM example, would you agree that competition would be enhanced if two railroads were able to compete for traffic?

Answer. With respect to the applicability to railroads of the essential facilities doctrine, I do not believe it does apply (nor do I believe it should apply) in the sense that a remedy for a railroad's refusal to grant trackage rights is generally available under the antitrust laws. Insofar as railroads are concerned, the Congress has dealt extensively with the matter of essential facilities in the Interstate Commerce Act and has provided adequate remedies where remedies are required. The Interstate Commerce Commission may compel the grant of trackage rights in a merger proceeding if deemed necessary in the public interest (49

U.S.C. §11344); it may compel the joint use of terminal facilities and mainline tracks for a reasonable distance beyond the terminal (49 U.S.C. §11103); it may authorize the construction or extension of a rail line across the lines of another carrier (49 U.S.C. §10907); it may compel the provision of facilities and equipment necessary to furnish safe and adequate car service (49 U.S.C. §11121(a)); it may compel the establishment of joint rates and through routes (49 U.S.C. §10705); and it may prescribe maximum reasonable rates where there is an absence of effective competition (49 U.S.C. §10701a(b)(1)). These provisions effectively subject potential "bottlenecks" to the jurisdiction of the Commission and give the Commission authority to fashion adequate remedies.

With respect to the question of access to the Toyota/GM plant, it would be inappropriate for me to comment on the merits of a matter of contention between members of the Association of American Railroads. I would note, however, that the dispute to which you refer is a good example of how the present regulatory remedies are adequate to determine whether regulatory intervention is necessary in order to enhance competition.

UP's proposal to construct a new track was the subject of an ICC proceeding and that proceeding was likely to be decided during the next few months. However, the parties requested a deferral to allow for a negotiated settlement between both railroads and the shippers which would resolve the issues to the satisfaction of the shippers. Latest reports are that a final settlement is very near. All of this was accomplished under the existing law.

Question 15. Under what section of Staggers did Congress explicitly recognize the principle of differential pricing?

Answer. The principle of differential pricing is explicitly recognized in the first policy pronouncement of the Staggers Act: "In regulating the railroad industry, it is the policy of the United States Government (1) to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail." (Section 101 of the Staggers Act enacting section 10101a of Title 49, U.S. Code). Pricing in accordance with the demand for services is differential pricing.

Question 16. Which Class I railroads are revenue inadequate?

Answer. In its latest determination (Ex Parte No. 457) the ICC found the following railroads to be revenue inadequate. The reason is apparent. Against a cost of capital in 1983 of 15.3 percent, the highest return on investment reported by any major railroad was 8.21 percent. The industry average was 3.88 percent.

Railroad	Return on Investment
Eastern District	
Baltimore & Ohio	0.02%
Bessemer & Lake Erie	2.28%
Boston & Maine	Not Available
Chesapeake & Ohio	4.08%
Conrail	3.71%
Delaware & Hudson	-6.75%
Detroit, Toledo & Ironton	-5.75%
Elgin, Joliet & Eastern	3.73%
Grand Trunk Western	-2.24%
Norfolk & Western	5.32%
Pittsburgh & Lake Erie	-10.44%
Southern District	
Alabama Great Southern	4.79%
Central of Georgia	8.14%
Cinc., New Orleans & Texas Pac.	9.71%
Florida East Coast	-5.38%
Illinois Central Gulf	-1.68%
Seaboard System Railroad	4.24%
Southern Railway	4.01%
Western Division	
Atchison, Topeka & Santa Fe	3.29%
Burlington Northern	8.21%
Chicago & North Western	4.74%
Chi., Milwaukee, St. Paul & Pac.	-1.05%
Denver & Rio Grande Western	2.91%
Duluth, Mesabi & Iron Horse	2.27%
Kansas City Southern	7.40%
Missouri-Kansas-Texas	6.53%
Missouri Pacific	4.88%
St. Louis Southwestern	3.33%
Soo Line	2.88%
Southern Pacific	-1.68%
Union Pacific	4.66%
Western Pacific	-10.16%

Question 17. Which Class I railroads or their affiliated companies have made non-railroad acquisitions since 1980? What were the companies, and what was the purchase price of each?

Answer. We do not compile data with respect to acquisitions by railroads or their affiliates. In an attempt to respond to your question we did review the Annual Reports of the Class I railroads (or their holding companies) for the years 1981-84. The following is a listing of the acquisitions as shown in those reports (excluding stock investments that do not result in a controlling interest):

RAILROAD	DATE	EVENT	AMOUNT $(MILLS)
BN	12/83	Acquired the El Paso Company	$ 1,300
CSX	8/83	Acquired Texas Gas Resources Corp.	1,110
NS	6/85	Acquired North American Van Lines (Pursuant to ICC authority)	315*

* Plus interest from 5/84 to 6/85

Question 18. Does a railroad have a legal obligation to reinvest profits earned from captive shippers in railroad facilities, or may that railroad invest the dollars earned in non-railroad ventures?

Answer. The only legal obligations with respect to the use of railroad income of which I am aware are those arising in connection with the incurrence of debt. In order to assure the payment of interest and repayment of principle, instruments of indebtedness may impose restrictions on the borrowing railroad. The ICC has, of course, issued orders compelling (or restricting) particular uses of funds as deemed necessary to the fulfillment of a railroad's common carrier obligations.

I would take issue with any implication that a "captive" shipper should have some special claim on the use of railroad income. A regulatory process exists to assure that for the rail service received a captive shipper pays no more than a reasonable rate. That is all that shipper or any other shipper is entitled to. It has no special claim against the way in which railroad earnings are utilized beyond the carrier's duty to provide adequate service.

Like every other private business in the United States, railroad management's first responsibility is to the shareholders whose assets it manages. It is management's job to seek the greatest return on those assets at the least risk. To the extent that earnings in the rail industry or any other industry are inadequate, management can and should be expected to look for alternative investment opportunities. Such investments will strengthen the railroad by smoothing out some of the peaks and valleys in the business cycle and thereby increasing the attractiveness of investment in the parent firm.

Question 19. Would you provide specific rates over the last five years for the movement of coal by unit train from the Powder River Basin to utility customers and from the Appalachian coal fields to eastern ports for exports?

Answer. The following compilations provided by the Burlington Northern, Chessie System and Norfolk Southern railroads provide complete or representative tariff rates for the movements requested. It is estimated that as much as 75 percent of export coal now moves under contract rather than the tariff rates shown. (Conrail, whose tariff rates are not shown, informs me that virtually all of its export coal moves under contract.) The data supplied by Burlington Northern indicates the same is true of coal moving out of the Powder River Basin. Consequently, the rates shown are, for the most part, higher than the rates under which coal is actually moving.

BURLINGTON NORTHERN RAILROAD COMPANY

REPRESENTATIVE UNIT TRAIN COAL RATES
($ per ton) as of Each July 1
Since Enactmment of Staggers Rail Act

(From Powder River Basin to Each Destination)

Destination	1981	1982	1983	1984	1985
Commonwealth Edison	18.39	20.34	21.58	22.88	*
Commonwealth Edison	21.02	23.25	24.48	26.16	*
KC Board of Public Utilities	13.49	14.92	15.75	16.49	16.49
Minnesota Power	9.35	10.34	10.93	11.29	*
Oklahoma Gas & Electric	13.27	14.68	16.96	18.32	*
Public Service Co. of Oklahoma	13.88	15.72	16.62	17.17	17.17
Portland General Electric	17.67	19.54	20.66	21.64	21.89
Southwestern Public Service	11.88	12.80	15.48	16.21	*
Houston Lighting & Power	22.92	24.33	24.57	25.73	*
Wisconsin Power & Light (Wyoming)	18.66	19.69	22.43	23.65	**
Wisconsin Power & Light (Montana)	13.96	15.44	17.49	17.49	*
Basin Electric	3.72	4.11	4.34	4.55	*
City Public Service Board of San Antonio	24.64	26.16	26.42	27.66	27.66

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* Currently under contract with Burlington Northern
** Currently under contract with Union Pacific/Chicago Northwestern

CHESSIE SYSTEM RAILROADS

EXPORT RATE HISTORY - BO CURTIS BAY COAL PIER, BALTIMORE, MD

Date	Ex Parte/ RCCR	ORIGIN			
		BO Cumberland-Piedmont; Somerset		BO - West Virginia, Gauley, Clay-Elk, Pittsburgh-Youghiogheny, Reynoldsville	
		Single Car	Trainload	Single Car	Trainload
1-01-81	X-386	R - 12.65 D - Included	-	R - 13.50 D - Included	-
7-11-81	X-002	R - 13.08 D - .45 13.53	-	R - 13.98 D - .45 14.43	-
9-07-81	X-002	R - 13.08 D - .73 13.81	-	R - 13.98 D - .73 14.71	-
1-01-82	X-082	R - 13.88 D - .77 14.65	-	R - 14.85 D - .77 15.62	-
3-14-82	X-082	R - 13.88 D - .77 14.65	① R - 13.64 D - .77 14.41	R - 14.85 D - .77 15.62	① R - 14.61 D - .77 15.38
1-01-83	X-083	R - 13.88 D - .78 14.66	① R - 13.64 D - .78 14.42	R - 14.85 D - .78 15.63	① R - 14.61 D - .78 15.39
1-13-83	X-083	R - 13.88 D - .77 14.65	① R - 13.64 D - .77 14.41	R - 14.85 D - .77 15.62	① R - 14.61 D - .77 15.38
8-27-83	X-083	R - 13.88 D - .77 14.65	① R - 13.48 D - .77 14.25	R - 14.85 D - .77 15.62	① R - 14.45 D - .77 15.22

Date	Ex Parte/ RCCR	ORIGIN			
		BO Cumberland-Piedmont; Somerset		BO - West Virginia, Gauley, Clay-Elk, Pittsburgh-Youghiogheny, Reynoldsville	
		Single Car	Trainload	Single Car	Trainload
1-01-84	X-084	R - 13.88 D - .77 14.65	① R - 13.48 D - .77 14.25	R - 14.85 D - .77 15.62	① R - 14.45 D - .77 15.22
1-01-85	X-084A	R - 13.88 D - .77 14.65	① R - 13.48 D - .77 14.25	R - 14.85 D - .77 15.62	① R - 14.45 D - .77 15.22

7-11-81 - Dumping separated from rate.
9-07-81 - Dumping charge increased.
3-14-82 - Trainload rates established.
1-13-83 - Dumping charge exempted from RCCR X-083 increase.
8-27-83 - Trainload rates reduced.

① - 7,000 N.T. (one origin) trainloads.

R = Rate
D = Dumping

EXPORT RATE HISTORY - BAY SIDE COAL PIER, CURTIS BAY
(BALTIMORE), MD.

Date	Ex Parte/ RCCR	ORIGIN			
		BO Cumberland-Piedmont; Somerset		BO - West Virginia, Gauley, Clay-Elk, Pittsburgh-Youghiogheny, Reynoldsville	
		Single Car	Trainload	Single Car	Trainload
3-14-82	X-082	12.54	① 12.31	13.51	① 13.26
1-01-83	X-083	12.54	① 12.31	13.51	① 13.26
8-27-83	X-083	12.54	① 12.14	13.51	① 13.11
1-01-84	X-084	12.54	① 12.14	13.51	① 13.11
1-01-85	X-084A	12.54	① 12.14	13.51	① 13.11

3-14-82 - Single Car and Trainload Rates to Bayside established.

8-27-83 - Trainload rates reduced.

① - 7,000 N.T. (one origin) trainload.

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Dumping in addition to above rates. Charges for dumping must be obtained from Bayside.

EXPORT RATE HISTORY - CONSOLIDATION COAL SALES COMPANY BALTIMORE
COAL TERMINAL, CANTON (BALTIMORE), MD.

Date	Ex Parte/ RCCR	ORIGIN			
		BO Cumberland-Piedmont; Somerset		BO - West Virginia, Gauley, Clay-Elk, Pittsburgh-Youghiogheny, Reynoldsville	
		Single Car	Trainload	Single Car	Trainload
6-30-83	X-083	12.54	① 12.31	13.51	① 13.26
8-27-83	X-083	12.54	① 12.14	13.51	① 13.11
1-01-84	X-084	12.54	① 12.14	13.51	① 13.11
1-01-85	X-084A	12.54	① 12.14	13.51	① 13.11

6-30-83 - Single Car and Trainload Rates to Consol established.

8-27-83 - Trainload rates reduced.

① - 7,000 N.T. (one origin) trainload.

Dumping in addition to above rates. Charges for dumping must be obtained from Consol.

EXPORT RATE HISTORY - CO PIER, NEWPORT NEWS, VA

Date	Ex Parte/ RCCR	ORIGIN					
		CO Group 1		CO Groups 2 & 3		CO Groups 4 & 5	
		Single Car	Trainloads	Single Car	Trainloads	Single Car	Trainloads
1-01-81	X-386	R - 13.58 D - .42 14.00	- -	R - 13.85 D - .42 14.27	- -	R - 14.18 D - .42 14.60	- -
1-01-82	X-082	R - 15.41 D - .77 16.18	- -	R - 15.72 D - .77 16.49	- -	R - 16.09 D - .77 16.86	- -
5-03-82	X-082	R - 15.41 D - .77 16.18	① R - 15.16 D - .77 15.93	R - 15.72 D - .77 16.49	① R - 15.46 D - .77 16.23	R - 16.09 D - .77 16.86	① R - 15.83 D - .7 16.6
1-01-83	X-083	R - 15.41 D - .78 16.19	① R - 15.16 D - .78 15.94	R - 15.72 D - .78 16.50	① R - 15.46 D - .78 16.24	R - 16.09 D - .78 16.87	① R - 15.83 D - .78 16.6
1-13-83	X-083	R - 15.41 D - .77 16.18	① R - 15.16 D - .77 15.93	R - 15.72 D - .77 16.49	① R - 15.46 D - .77 16.23	R - 16.09 D - .77 16.86	① R - 15.83 D - .7 16.6
8-27-83	X-083	R - 15.41 D - .77 16.18	② R - 15.01 ③ 14.81 D - .77 .77 15.78 15.58	R - 15.72 D - .77 16.49	② R - 15.32 ③ 15.12 D - .77 .77 16.09 15.89	R - 16.09 D - .77 16.86	② R - 15.69 ③ 15.4 D - .77 .77 16.46 16.2
1-01-84	X-084	R - 15.41 D - .77 16.18	② R - 15.01 ③ 14.81 D - .77 .77 15.78 15.58	R - 15.72 D - .77 16.49	② R - 15.32 ③ 15.12 D - .77 .77 16.09 15.89	R - 16.09 D - .77 16.86	② R - 15.69 ③ 15.4 D - .77 .77 16.46 16.2
1-01-85	X-084A	R - 15.41 D - .77 16.18	② R - 15.01 ③ 14.81 D - .77 .77 15.78 15.58	R - 15.72 D - .77 16.49	② R - 15.32 ③ 15.12 D - .77 .77 16.09 15.89	R - 16.09 D - .77 16.86	② R - 15.69 ③ 15.4 D - .77 .77 16.46 16.2

1-13-83 - Dumping charge exempted from RCCR X-083 increase.

① - 7,000 N.T. Trainload rate (1 origin) (Established 5/03/82)
② - 7,000 N.T. Trainload rate (1 origin) (Reduced 8/27/83)
③ - 10,000 N.T. Trainload rate (1 origin) (Established 8/27/83)

R = Rate
D = Dumping

EXPORT RATE HISTORY - MASSEY COAL TERMINAL - PIER 9,
NEWPORT NEWS, VA.

Date	Ex Parte/ RCCR	ORIGIN					
		CO Group 1		CO Groups 2 & 3		CO Groups 4 & 5	
		Single Car	Trainloads	Single Car	Trainloads	Single Car	Trainloads
1-28-83	X-083	13.67	① 13.43	14.00	① 13.75	14.35	① 14.11
8-27-83	X-083	13.67	① 13.27 ② 13.07	14.00	① 13.60 ② 13.40	14.35	① 13.95 ② 13.75
1-01-84	X-084	13.67	① 13.27 ② 13.07	14.00	① 13.60 ② 13.40	14.35	① 13.95 ② 13.75
1-01-85	X-084A	13.67	① 13.27 ② 13.07	14.00	① 13.60 ② 13.40	14.35	① 13.95 ② 13.75

1-28-83 - Single Car and Trainload rates to Massey established. (NOTE: Rates to Massey expired 2-04-83 and were reinstated 2-07-83.)

8-27-83 - 7,000 N.T. Trainload rates reduced. 10,000 N.T. (one origin) Trainload rates established.

① - 7,000 N.T. (one origin) Trainload.
② - 10,000 N.T. (one origin) Trainload.

Dumping in addition to above rates. Charges for dumping must be obtained from Massey.

Norfolk Southern's Export Coal Rates ($/ton)*

From	To		To		To		To	
	Lambert's Point		Baltimore		Philadelphia		Port Reading	
Group #	1981	1985	1981	1985	1981	1985	1981	1985
NW Group 3					17.73M	21.91M		
NW Group 3	13.58	15.41	18.42	22.77	19.50S	24.11S	20.48	25.31
NW Group 4					17.73M	21.91M		
NW Group 4	13.85	15.72	18.42	22.77	19.50S	24.11	20.84	25.31
NW Group 5					18.52M	22.90M		
NW Group 5	13.85	15.72	19.27	23.83	20.39S	25.21S	21.32	26.35
NW Group 6					18.52M	22.90M		
NW Group 6	13.85	15.72	19.27	23.83	20.39S	25.21S	21.32	26.35
Sou Group 6					23.45M	28.97M		
Sou Group 6	13.85	15.72	24.14	29.83	25.22S	31.17S	26.20	32.37
Sou Group 6A					18.97M**	23.46M**		
Sou Group 6A	13.85	15.72	19.32	23.83	24.00S	29.68S	24.98	30.88

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* Excludes dumping charges
** To Fairless, PA
M = Metallurgical coal
S = Steam Coal

ICF INCORPORATED International Square 1850 K Street Northwest Washington D C 20006 (202) 862-1100

July 26, 1984

MEMORANDUM

TO: Rob Brenner

FROM: Daniel E. Klein
Hoff Stauffer

SUBJECT: Transportation Rate Assumptions for Coal Market Forecasting

In recent years, railroads have gained considerable flexibility in pricing rail services. The Staggers Rail Act and subsequent ICC regulations have enabled carriers to price their services more on the basis of market value than on the basis of carrier costs.

This paper discusses the conceptual basis for representing future coal transportation rates in making coal market forecasts. Specifically, we discuss why it is more appropriate to employ **marginal** rates rather than industry-wide **averages** and why the marginal rate is less than an average rate. We also discuss the implications of this assumption in assessing alternative acid rain mitigation programs.

USE OF TRANSPORTATION RATES IN COAL MARKET FORECASTING

Transportation rates play an important role in analyses and forecasts of the energy markets. This role is particularly critical in the coal markets, where transportation costs for coal account for a substantial portion of the delivered fuel costs. In the marketplace (and in coal market forecasting approaches as employed by ICF), fuel consumers seek to minimize delivered fuel costs,[1] subject to quality constraints, environmental regulations, and contract obligations. Different types of coals and different coal supply regions are in competition for the various coal demands. Transportation rates will affect the relative competitiveness of one region and/or type of coal vis-a-vis others.

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[1] Fuel costs here are defined to include differential burn and pollution control costs. For example, if a higher sulfur coal required a scrubber, the cost of the scrubber would be added to the delivered price of the higher sulfur coals in comparison with lower sulfur coals which do not include scrubbers. A simpler example is that additional ash disposal costs would be added to the cost of a higher ash coal.

Recent analyses of coal markets have made a wide range of assumptions regarding future transportation rates. Some analyses have assumed that transportation rates, particularly rail transportation rates, would increase considerably in future years as railroads exercise their market pricing powers in an effort to become revenue adequate.

ICF assumes that on the margin rail transportation rates will decrease. Our reasoning is described below.

This assumption has significant implications for coal market forecasts. Under lower marginal rates, the number and distance of competitive supply alternatives available to any particular source will increase. In addition, the competitiveness of more distant lower sulfur coals is improved relative to retrofit scrubbing nearby, higher sulfur coals.

COMPETITION IN RAIL TRANSPORTATION

In the marketplace, "competition" is a relative rather than an absolute term. Rarely does the situation exist that there are absolutely no alternatives available at any price. Instead, there are often one or more alternatives available, although some may be very costly. The presence or absence of "competition" on a particular movement is thus ultimately a judgment as to how close are the various alternatives in terms of price.

Several types of competitive alternatives may exist for particular movements:

- **Transportation competition** -- There may be two or more railroads serving the route (intramodal) or other transport alternatives such as truck or barge (intermodal).
- **Source competition** -- Alternative sources of coal (either from other mines in the same region or from other regions) can be shipped via different carriers.
- **Product competition** -- Other fuels (e.g., wood waste, natural gas) may be substituted for coal in the boiler and/or power generated from other stations may be substituted to some extent for power generated from a specific station.

Of course, many of these potential alternatives may not exist for a particular plant, particularly in the near term. Coal supply contracts may not permit flexibility in sourcing the coal. Alternative transportation receiving facilities may not be in place. Access to alternative fuels and/or power from other plants may not be available at all or only at a very high price.

Over time, the alternatives available to a plant may broaden. Coal supply contracts may expire, enabling coal sourcing from other regions and carriers. Alternative transportation facilities (e.g., barge, pipeline) may be constructed. New plants may be sited to provide flexibility in receiving from more than one carrier. Some utilities may be able to use the threat of longer term competition or of competition at another station in order to negotiate more favorable treatment for an otherwise captive station.

DIFFERENTIAL PRICING

Railroads are a capital intensive industry. Fixed costs are a significant expense in running the system and include such items as investment in and maintenance of the main-line track. A railroad should seek to have its rate for each movement cover at least variable costs and to have the collective contribution above variable costs from all movements to cover at least its fixed costs (including a fair market return of and on capital). So long as a particular movement can at least cover its variable costs, it is making some contribution to the fixed costs of running the system. A railroad would obviously like to carry a movement at the highest rate possible, but would be willing to accept rates at a level which provide some small contribution to fixed costs rather than not to have the movement at all.

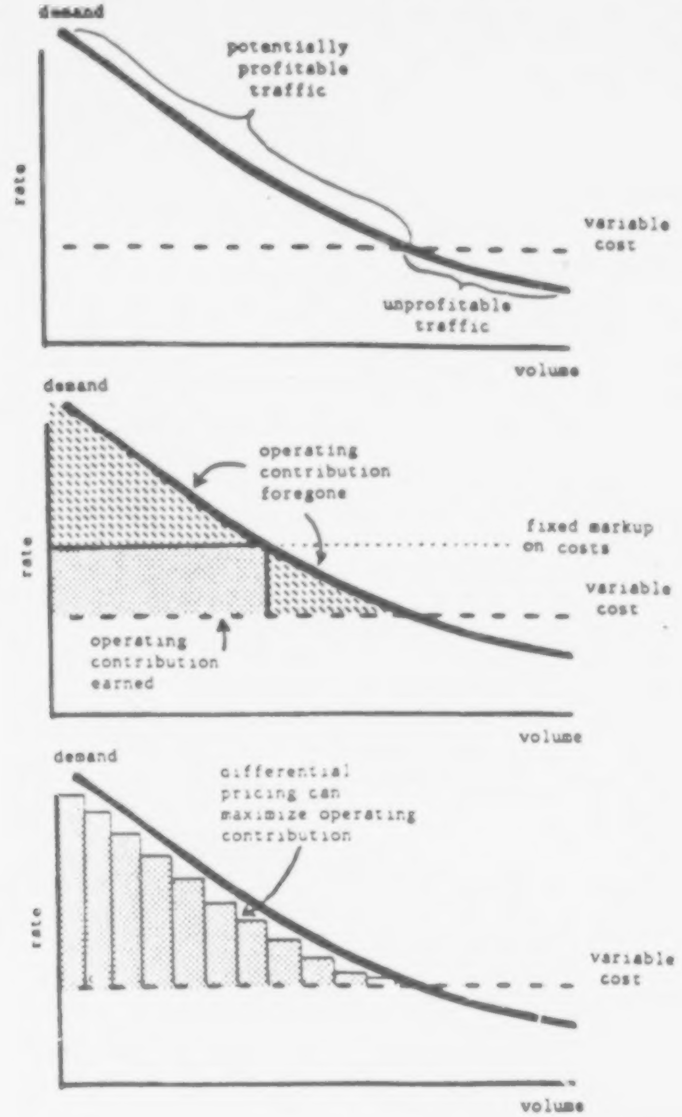
For some movements, a railroad might not face much competition. Hence, it would want to raise its rate, if permitted, up to the delivered price of the next best alternative. This could be a substantial increase. In so doing, the railroad would maximize the contribution to fixed costs made by this movement. However, it would not be in the railroad's best interest to raise the rate so high that the shipper would prefer some other alternative, since there would then be no contribution to fixed costs.

On other routes, competition may be intense. Two or more railroads may serve the same route. Trucks or barges may also compete. The consumer may have alternatives available from other mines and carriers. In such situations, competition will drive down rates and keep them low. The carrier with the lowest variable costs will tend to capture the traffic. As long as the rate can cover variable costs and make some contribution to fixed costs, it will be seen as desirable to the carrier.

Railroads can differentially price among movements. They have incentives to price low when faced with competition and price high when little competition exists. Consider Figure 1, which depicts a hypothetical demand for rail services as a function of rates. The horizontal line labeled "variable costs" is a level below which the railroad could not generate a contribution to fixed costs. In order to become revenue adequate, the railroad must generate enough of a contribution (the area between the variable cost line and the demand curve) to cover fixed costs (including a return of and on capital). Obviously, any constant markup over variable cost (middle figure) would (1) entail a loss of desirable traffic which could have made at least some contribution and (2) fail to maximize the contribution on other traffic. By pricing each movement differentially (bottom figure), charging more or less depending on competition for each movement, the railroad can maximize the contribution to fixed costs.

FIGURE 1

DIFFERENTIAL PRICING FOR A RAIL SYSTEM



ICF INCORPORATED

A railroad will charge just a little bit less than the costs of the next best alternative, so long as this covers variable costs. Therefore, variable costs will determine the minimum rate a carrier will be willing to consider. The cost of alternatives to the shipper will tend to determine the maximum rate that can be sustained. Where few or no competitive alternatives exist, transportation rates will increase considerably. Where competitive alternatives exist or can be generated, carriers will have much less power to increase rates and could be forced to lower them, lest the traffic be lost.

AVERAGE RATES

Many analytic approaches for forecasting coal market activities employ some form of a coal transportation network. These networks will typically link together coal supply origins with coal demand destinations. Origin-destination routes are then described using several parameters, in particular the transportation mode and mileage.

These transportation network descriptions are typically then assigned rates in order to enable comparison of different routes and modes. Underlying this step is the notion that the physical attributes of a movement will determine its costs and hence influence its rate. One common approach for doing this is to develop regression equations from a set of existing tariffs. Elements which have been shown to influence costs include mileage, region of origination, single car versus unit train, single carrier versus joint hauls, car ownership, and difficult terrain.

These regression equations cannot explain all of the variations among rates. Some will be higher than predicted, some lower. These variances may reflect the presence or absence of competitive alternatives on specific movements. Where competitive alternatives exist, rates could be expected to be less than average. Conversely, where alternatives are less competitive, rates may be higher than average.

Some have argued that deregulation and the railroads' subsequent attempts to achieve revenue adequacy will lead to an across-the-board increase in rates beyond increases in costs of service. This assumption directly contradicts the observation that for individual movements, a railroad would rather carry the traffic at a low rate and still make some contribution to fixed costs rather than lose the movement all together.

Because railroads can price differentiate, they have strong incentives under deregulation to raise rates for less competitive movements while keeping rates low where competition is strongest. To assume that railroads would raise rates across the board without concern for market consequences (i.e., diversion of profitable traffic) assumes that at least one of the following conditions must hold:

1. Each railroad has market power over all of the movements it can serve. While this may be true for some movements, it is certainly not true for all. Further, if this condition were true, there would be no need for coal market models which were based upon competitive market conditions and permit shifts in coal sourcing.

2. Carriers are acting in collusion. Even if this were a legal option, there is little evidence to suggest that it may be true. Further, many railroads are in competition with barges, trucks, and/or coal slurry pipelines, all of whom tend to have little incentive to enter into collusive arrangements with the railroads.

3. Each railroad, acting independently, mindlessly raises its rates irrespective of the diversion of traffic. While railroads have strong incentives to raise rates where there is little or no competition, they also have strong incentives to keep rates low where competitive pressures exist. To raise rates mindlessly beyond the point where diversion to other carriers would occur would reduce the contribution to fixed costs substantially. Further, shippers who would be affected by such mindless rate-making would have strong incentives to inform the railroad of its impending loss of traffic before it switched to alternative carriers.

MARGINAL RATES

In ICF's recent forecasts, we have assumed that **marginal** rail transportation rates will approximate **long-run variable costs**. This represents the level that a railroad should be willing to accept in order to avoid losing a particular movement to a competing carrier and/or mode.

Specifically, we are assuming that on the margin, future rail transportation rates will be about 95 percent of current averages. Our analyses to date indicate that long-run variable costs are at least five percent less (in real terms) than current average rates, after accounting for real escalation in costs such as fuel.

However, more rigorous estimates of long-run variable costs are warranted. Our judgement is that they could be lower than the estimates we are currently using.

For other transport modes, particularly barge and truck, we are assuming that competitive pressures are already reflected in current rates and that future rates will change primarily to reflect cost changes in fuel prices and other components.

SUPPORTING EVIDENCE FOR COMPETITIVE MARGINAL RATES

Railroad ratemaking gained considerable flexibility under the 4-R Act of 1976 and gained momentum with the passage of the Staggers Rail Act in 1980. As the railroads have moved further into a deregulated environment, there have been increasing opportunities to observe railroad pricing behavior relative to the conceptual arguments presented earlier.

Changes in Average Rates

Although many rail movements have shown substantial changes (both up and down), there is little evidence to suggest that deregulation is leading to widespread increases in rail rates above the underlying costs. Consider Figure 2, which graphs an index of railroad costs (the AAR Railroad Cost Recovery Index) to an index of coal rail rates (the PPI rail freight transportation index for coal). Between 1977 and 1983, costs rose at an average annual rate of 9.3 percent, while rates rose at a 9.7 percent rate. Since the passage of the Staggers Rail Act in October 1980, railroad costs have increased at a 6.8 percent annual rate, while rates have increased at a 6.6 percent annual rate.

The AAR Railroad Cost Recovery Index has been the subject of some controversy. Critics of the index have cited the index's failure to adjust for productivity changes and its use of escalation factors which do not accurately track changes in component costs. Alternative formulations for railroad cost indices have been offered which suggest cost increases one to two percent per year less than the AAR Index. To the extent that these alternative formulations may be more reflective of true changes in total costs, the difference between rate increases and cost increases would be more substantial than shown in Figure 2. However, this possible increase in real rates over costs is still well below levels permitted under the Staggers Act and subsequent rulings.

Changes In Specific Movements

The effects of competition on railroad pricing behavior can best be understood by examination of several recent situations.

- TVA's Gallatin Plant

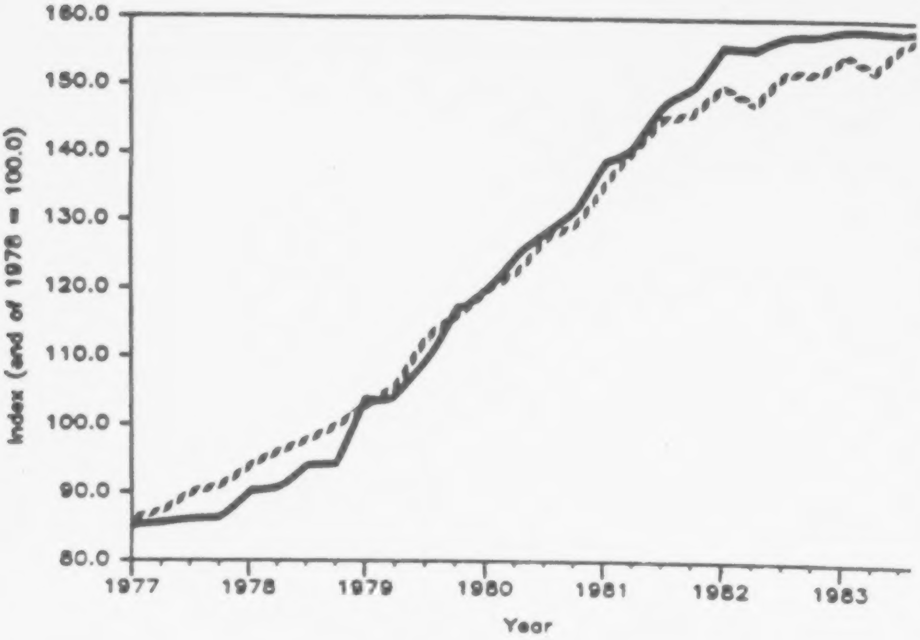
TVA's Gallatin plant in Tennessee consumes about 3 million tons of western Kentucky coal per year. Coal deliveries were made by the L&N. L&N had been railing the coal about 100 miles to a junction in the town of Gallatin, from which point TVA used its own engines and rolling stock to move it the rest of the way to the plant. L&N's rates were about 9 dollars per ton.

In 1982, TVA began installing a temporary barge unloader on the adjoining Cumberland River in an effort to increase its flexibility in coal deliveries. The planned barge facility would allow TVA to unload about 3,000 tons per day. A TVA spur would carry the coal from the barge unloader to the plant. The barges on the Cumberland River would provide direct competition to the L&N by carrying the same coal that Gallatin had been receiving already. In addition, the barges provided an additional option of receiving coal diverted from other TVA plants in Johnsonville and Cumberland which also have rail and barge flexibility.

During the year that TVA was planning the installation of the temporary barge unloader, rail rates on the L&N declined from about $9 per ton to about $5 or $6 per ton.

FIGURE 2

RAILROAD COSTS VS. RATES, 1977-1983
(end of 1978 = 100.0)



AAR, Railroad Cost Recovery Index

PPI, Railroad Freight Transportation Index for Coal

ICF INCORPORATED

- Arkansas Power and Light's White Bluff and Independence Stations

Until recently, the Burlington Northern (BN) was the sole originator of coal coming out of the Powder River Basin in Wyoming and Montana. In a long-running legal and regulatory battle, the Chicago and Northwest railroad (C&NW) has been working toward obtaining rights to originate coals in the southern part of the Powder River Basin. These C&NW originations would then be passed on to the Union Pacific (UP) as a competitive alternative to the BN. In addition, the proposed ETSI pipeline has been working toward obtaining the necessary permits and contracts to construct a coal slurry pipeline from the Powder River Basin to markets in the West South Central region.

For its new stations at White Bluff and Independence, Arkansas Power and Light was able to create a 3-way transportation competition among BN, C&NW, and ETSI. As a result of this competition, a 20 year transportation contract was signed with the C&NW and UP. This contract involves rail movement of about 10 million tons per year.

Precise contract rates were not disclosed but are believed to have been a substantial reduction below current rates on similar movements. Arkansas Power and Light estimated that the contract would provide savings of over 200 million dollars by the end of 1986, and about $16.5 billion through the year 2016. Some analysts have estimated these savings to be on the order of 30 to 40 percent.

- Cajun Electric Power Cooperative's New Roads Plant

In October 1983, Cajun Electric Power Cooperative and Burlington Northern announced the signing of a 15 year contract for shipment of Powder River Basin coal to Cajun's New Roads plant in Louisiana. The coal would be shipped by BN to a transfer facility in St. Louis, beyond which barges would deliver the coal.

In negotiating the transportation contract, Cajun Electric considered many approaches. Since its current coal supply contract with Shell is for coal which originates in the northern portion of the Powder River Basin accessible only to BN, Cajun considered altering the existing coal supply contract. Additional alternatives considered included changing mine sites to another Shell mine accessible to the C&NW, evaluating coal slurry pipeline alternatives, and others.

As with most rail contracts, exact contract terms are confidential. However, Cajun estimated that its new contract would save them a minimum of 500 million dollars over the 15 year contract life. An official at Cajun indicated that of the coal rates with which they were familiar, their's was clearly at the lowest level.

- Northern Indiana Public Service Company's Schahfer Plant

After the Medicine Bow Mine in the Hannah Basin had its coal supply contract terminated due to coal quality problems, Northern Indiana Public Service Company (NIPSCO) contracted for coal supplies from the Orchard Valley

Mine in Converse, Colorado. Under the original tariffs, coal was moved from the mine to NIPSCO's Schahfer plant at Wheatfield, Indiana, over a 1500 mile route. The coal originated on the D&RGW and terminated by Conrail, with the Sante Fe acting as a bridge carrier.

NIPSCO opened up the bidding to the railroads in order to obtain better rates and service agreements. For this movement, there were fewer competitive alternatives available on the origination and termination. However, alternatives existed for the bridge carrier, where UP could also act as the bridge carrier either alone or in combination with the C&NW.

New tariffs were published in May 1983, reflecting changes in both rates and service agreements. The new tariff provided for reductions in rates for higher annual volumes than those stated in the earlier tariff. In addition to the volume incentive rates, routings were changed to reflect UP and C&NW replacing the Sante Fe as the bridge carrier.

- **New York State Electric & Gas**

In 1983 New York State Electric & Gas signed a transporation contract with Conrail that would increase the proportion of coal which the utility takes by rail. NYSEG's Greenidge, Goudey, and Milliken plants in the southern tier of New York had formerly taken coal by Conrail as well as substantial deliveries by truck.

Conrail agreed to new volume incentive rates and also agreed to the necessary track investments to support this increased traffic. Under the new volume incentive rates, Conrail would carry much of the coal traffic which had formerly been carried by truck. During the negotiation with Conrail, NYSEG shifted all of its coal transportation to truck. NYSEG noted that the contract with Conrail would reduce transportation costs significantly.

- **Jacksonville Electric Authority's St. Johns River Power Park**

The St. Johns River Power Park of Jacksonville Electric Authority will consume about 3 million tons of coal per year when it begins operation in 1987. The utility is presently in the process of evaluating its coal supply alternatives.

St. Johns is located on a Seaboard System rail line, and any rail deliveries of coal would have to move on at least part of the Seaboard System. However, the utility is also considering water delivery as well, where an unloading facility would be coupled with the plant by a closed conveyer system of about 2.5 miles. It is their belief that rail rates are 15 to 25 percent higher when water competition does not exist.

- **Virginia Electric Power Company**

Vepco's Virginia plants receive coal on the Norfolk Southern or CSX Lines. Vepco and others have been promoting legislation which would permit the construction of coal slurry pipelines in Virginia. The slurry pipeline proposals have met with great opposition from the railroads and others.

Concurrent with their efforts to enable development of coal slurry pipelines, Vepco has pursued rate reductions on its railroad delivered coal. In June 1984, Vepco estimated that as a result of a new contract with the CSX and the negotiated rate reduction with Norfolk Southern, its rail costs savings for its Virginia plants would be 9 million dollars annually.

- San Antonio Public Service's Deely Plant

San Antonio Public Service is presently in the process of negotiating coal transportation service for the J. T. Deely plant. The present rate is $27.56 per ton for a 1652 mile movement. In March 1984, five transportation contract bids were submitted to the utility. Four of the bids were from different railroads (or combinations of railroads), and the remaining bid was from the ETSI Pipeline.

The low bids were more than 10 percent below the current rate. The BN proposal offered coal movement at $24.43 per ton, or 89 percent of their current rate. The ETSI proposal called for a slightly higher rate of $24.90 per ton, but provided additional economic benefits in the form of 25 megawatts of cogenerated power to be supplied from the slurry dewatering facility.

As of June 1984, San Antonio had not yet selected any of the transportation bids. The utility is also pursuing favorable regulatory treatment from the ICC in enforcing a special amendment to the Staggers Act which limited rates for San Antonio to 162 percent of variable costs.

- ICF Experience

In addition, ICF has assisted two electric utility clients in coal procurement and transportation strategies. By generating direct competition (e.g., truck) or indirect competition (e.g., barge to another station and offer a "package deal"), our clients were able to negotiate contract rates below current tariffs.

INTERPRETATION

The use of marginal rail rates is most appropriate for forecasting origin-destination flows, regional coal production, and mine-mouth prices. The carrier with the lowest costs will be able to capture the movement. The use of marginal rates in coal market forecasting ensures that each movement will be captured (in the forecasts) by the least-cost mode and route, where costs include delivered fuel costs plus differential burn and pollution control costs. Hence, the origin-destination flow forecasts will be correct. Because of the structure of the model, forecasted coal production, mine-mouth prices, and coal utilization will also be correct, except for certain second-order effects discussed below.

Conversely, use of higher rates (such as average rates or escalated average rates) would not ensure that the forecasted movements would reflect the least-cost mode and route. This is because such higher rates are generally computed as a multiple of variable costs. Hence, the absolute increase in movements with higher transportation costs is greater than for movements with lower transportation costs, creating a substantial bias against longer-hauls which, of course, generally have higher transportation costs.

Our assumption of cost-based marginal rates for forecasting does not imply that railroads will actually offer marginal rates all the time. Some movements face limited competition and are subject to rates which are higher than marginal costs. As deregulation proceeds, such movements will be vulnerable to rate increases, perhaps even substantial rate increases, as we have discussed earlier, up to the delivered price of the next best alternative. For such movements, the marginal rate assumption will understate the delivered costs but will not distort the origin-destination pattern of coal shipments because the railroad should not increase the rate to the extent that the movement would shift to an alternative mode, route, or carrier.

No Loss in Welfare

The higher rate reflects a transfer of welfare from the consumer to the carrier. However, since such transfers do not affect the origin-destination patterns of coal shipments, total economic costs to society are unchanged.

The shift in welfare from consumers to railroads is not a loss in welfare to society. Recent rail legislation and deregulation is justified properly with the argument that rails must earn an adequate market rate of return on invested capital to be viable in the long-run and that our economy needs railroads. Hence, such shifts from consumers to railroads help in achieving another important national goal - a financially sound railroad network.

The conceptual economic arguments in favor of permitting the railroad to price discriminate - Ramsey pricing - implies rate of return regulation once railroads become revenue adequate. This linkage has not yet fully entered the legislative or regulatory debates, but probably will. If rate of return regulation is installed when railroads become revenue adequate, situations that permit railroads to earn higher margins over marginal (or long-run variable) costs will not increase railroad revenues but rather reduce rates to other consumers. Hence, the shift in welfare would be from one coal consumer to other consumers, rather than to the railroad.

Second-Order Effects

Although cost-based marginal rates tend to capture properly distribution patterns and hence total national costs, there are some circumstances in which second-order impacts may not be adequately reflected. These second-order impacts could result when delivered prices are above costs. For some utilities, these higher delivered costs for less competitive movements could affect the dispatching sequence for a utility system, causing load to to be shifted to other units. In addition, the higher costs of generation would lead to higher electricity rates which in turn would lead to lower demands for electricity, thereby tending to reduce total fuel requirements.

Both of these potential situations represent circumstances under which a particular movement is not necessarily captured or lost in its entirety, but rather the carrier sees some form of a downward sloping demand curve for that particular movement. In such situations, a carrier may use monopoly pricing, where the carrier can increase profits by setting higher rates such that some portion of the traffic which he would capture with a lower rate would be foregone, in order to earn higher margins on the rest of the traffic.

These second-order effects are probably not substantial. However, this hypothesis could and probably should be tested.

IMPLICATIONS FOR ACID RAIN ANALYSES

In analyses of many air pollution control questions, particularly proposed acid rain mitigation measures, the level of rail rates used takes on particular significance. Under many proposals, utilities and possibly other coal consumers would need to reduce sulfur dioxide emissions, primarily through switching to lower sulfur coals or retrofitting scrubbers. Plants now burning higher sulfur coals typically are sited closer to higher sulfur coal fields. Shifts to lower sulfur coals typically entail longer distance movements of coal replacing more nearby sources.

Under assumptions of across-the-board increasing rail rates, these more distant lower sulfur coals would show a greater increase in delivered costs than would nearby higher sulfur coals, thereby making shifts to lower sulfur coals less attractive.

In analyses of acid rain mitigation measures, cost-based marginal rail rates will properly capture shifts in coal markets, changes in mine-mouth prices of coal, and total national costs. However, since not all movements of coal are actually transacted at this rate, the delivered prices for the less competitive movements would be understated.

Overall, consumer cost impacts would be understated in both a base case and acid rain case to the extent that less competitive movements exist. It can not be stated a priori that the excess of rail revenues over marginal costs would be either higher or lower under particular acid rain proposals.

For example, powerplants in New York are closer to the high-medium sulfur coals in Pennsylvania than to the low sulfur coals of southern West Virginia and eastern Kentucky. These powerplants are currently permitted to burn high-medium sulfur coals. Only one railroad serves these stations and the Pennsylvania coal fields. The rail rates from Pennsylvania have been set substantially above marginal costs at about the level of the next best alternative, which is truck. If these powerplants were forced to reduce emissions, they might be able to generate increased transportation competition, since other railroads serve southern West Virginia and eastern Kentucky. Hence, the cost of rail transportation might increase - because the low sulfur coal would travel further - but the excess of the rate over marginal cost could decrease because of increased competition.

Alternatively, a powerplant might be able to generate rail competition for higher sulfur coals but not for lower sulfur coals.

But the fundamentals remain. The low cost option will be able to win the movement, although the rates will tend toward the cost of the next best alternative. ICF's use of marginal rates will forecast origin-destination flows correctly and except for second-order effects discussed above will forecast coal production, prices, and utilization correctly. Consumer costs will tend to be understated, in both the base case and the acid rain case. This is because consumers will pay delivered costs reflecting rates based on the marginal costs of the next best alternative, rather than of the least-cost alternative. Rail revenues, correspondingly, will be understated.

The change in the understatement of consumer costs and rail revenues between a base case and/or acid rain case has not been determined. It could be higher or lower depending on the specifics of each powerplant. Case studies could elucidate this issue.

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Senator McConnell. And our final witnesses appearing as a panel, Fred Palmer general manager of Western Fuels Association and Robert Bergland, executive vice president of the National Rural Electric Cooperative Association.

STATEMENT OF FRED D. PALMER, GENERAL MANAGER WESTERN FUELS ASSOCIATION, INC., WASHINGTON DC; AND BOB BERGLAND, EXECUTIVE VICE PRESIDENT, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION, WASHINGTON, DC

Mr. Bergland. Mr. Chairman, members of the committee, my name is Bob Bergland and I am the general manager of the National Rural Electric Cooperative Association. We are a national service organization for 1,000 consumer-owned, not-for-profit electric systems in 46 States, and we serve 25 million persons who live in rural places.

I am pleased to be here today to support the bill under consideration, S. 447, which offers the promise of equalizing the bargaining positions between coal users, such as electric utilities, and the railroads.

Our members and their consumer owners have been adversely affected by coal transportation costs and we feel quite strongly about this issue. Coal is the major fuel source for generating electricity that our own members produce. Of about 1,000 local systems, some 62 are generation and transmission cooperatives, which generate and/or transmit electric power.

As of January of this year, about 78 percent of that generation was from coal and lignite for a total of 21,505 megawatts. Additional power is purchased by our members from outside generators, much of which is coal fired. Anything that affects the price of coal at the generating station affects our members. While the price of coal has remained relatively stable for several years, the delivered cost of coal, because of excessive railroad freight rates has continued to climb, raising the cost of electricity to our individual members.

Transportation costs are, of course, directly passed through in the form of higher electric rates, and rural electric cooperatives already pay rates that are about 15 percent higher than that of competing utilities on a nationwide basis.

Due to the concern that we have over these matters, our association has been active for many, many years in transport issues. We were, of course, very involved in the legislative package that was developed in 1980, entitled the Staggers Rail Act. Unfortunately, the interpretation of that act by the ICC, through its numerous rulemakings has resulted in upsetting the careful balancing of interests originally intended by Congress.

While the ICC has pursued the goal of maximizing railroad revenues, with a zeal that every profit-making business would envy, it has virtually ignored those provisions, such as the Long/Cannon amendment which Congress built into the act, in order to balance the interests of shippers and carriers. The bias of the Commission is illustrated most starkly by the Commission's proposal to limit rail rates on captive coal traffic only when the rate exceeds the cost to the shipper of building and operating its own railroad ("stand alone costs").

During the same time period in which there has been a deterioration in regulatory protection for captive shippers, there has also been a dramatic increase in concentration of rail market power. Mergers between railroads have further reduced what little competition was previously available. The bill before the committee today would introduce an element of competition into the monopoly market. It provides that a shipper or other railroad can have an alternative for the shipment of coal by using the tracks of the monopoly railroad.

S. 447 will provide both competition and a yardstick by which to measure the true cost of providing rail service. By creating a competitive environment, increased efficiencies of service will be encouraged and competition will shape the marketplace.

In my opinion, the granting of access to tracks is essential to railroad competition in the rail industry and a critical lever to encourage effective, ongoing bargaining between the carrier and the shipper.

Most of our members that have coal needs are also members of Western Fuels Association, and I will yield to Fred Palmer, who is with me today on the panel, for the specifics regarding their transportation problems.

Mr. Chairman, We compliment you and members of this committee for raising this most important subject and we will do everything that we can to help you find an answer to this dilemma. Thank you.

STATEMENT OF FRED D. PALMER

Mr. PALMER. Thank you, Mr. Chairman, and good morning.

First of all, Mr. Chairman, I have with me this morning, Orren Beatty, who is our manager of communications and governmental affairs on our right. Orren has distributed a prepared statement under my name and I would ask that it be incorporated into the record.

Senator McCONNELL. Without objection, that will be put into the record.

Mr. PALMER. Thank you, sir.

My name is Fred Palmer and I am the general manager of Western Fuels Association. We produce, buy, and distribute coal and we are a cooperatively owned fuel supplier to consumer-owned electric utilities, including rural electric cooperatives and municipal utilities. We are a national organization with headquarters in Washington, DC, and our 35 members service areas extend into every State west of the Mississippi River; large areas of the southeast and Puerto Rico.

Mr. Chairman, in 1984, we supplied fuel to nine different power plants in different parts of the country and we delivered in excess of 10 million tons of coal to those plants.

In 1984, we paid $83 million in transportation charges, primarily to five class 1 railroads. We are in the transportation market continually and constantly and we think that we understand it and we are in that part of the market that Mr. Dempsey refers to as the 15 percent that is not competitive and that is why we are here today.

I have heard Mr. Dempsey say on many occasions and I have read statements by the Association of American Railroads on many occasions that the price of coal has increased faster at the mine than the price of transportation of that coal and I must say, I am baffled because we buy coal all over the country, we are in the coal market all over the country and it has been the opposite of our experience.

Today, in 1985, for example, you can buy coal in Wyoming's Powder River Basin for less in nominal terms, for under $6 a ton let us say, than you could in 1975 or 1976. The cost of transporting that coal, since 1976 has increased in real terms by over 40 percent and that suggests only one thing to me, Mr. Chairman, that is that the railroad market in that part of the country has been inherently anticompetitive and that it has hurt the coal industry dramatically, and that it certainly has hurt the customers of Western Fuels and the rural consumers who purchase electricity from our members.

Our experience in the market shows us that there are any number of abuses. First with respect to price, there is no question in our mind that monopoly pricing occurs in most situations where large volumes of coal move over class one railroads.

The Consumer Federation of America has estimated that over $1 billion in overcharges have been levied on coal producers by class one railroads. Service has deteriorated in many of our movements, Mr. Chairman, and I attribute this again, to a monopoly situation. A competitive environment produces competitive service, which means good service, and without competition, the monopolist is allowed to provide poor service, and we have suffered from that. The railroads that we have dealt with in some instances have refused to provide quotes for us from junction points to destination areas, where competition would exist or vice versa, from the end of a movement, a junction, to a powerplant where competition is eliminated in the first part of the movement.

We, again, believe that this establishes the existence of monopoly power. Much has been said this morning about the changed regulatory environment and the fact that the Interstate Commerce Commission no longer regulates. It does not and everybody in this room knows that it does not. It exists and operates under a statute that allows a wide latitude of monopoly pricing by the railroads in the first instance, and the Interstate Commerce Commission has taken the discretion that it has under the act, to completely deregulate. If you are in the coal business, if you are subject to monopoly by a railroad and you are interested in getting relief, the last place that you would look to is the Interstate Commerce Commission, it does not regulate.

The antitrust laws, possibly, are an alternative under existing law for shippers and shippers of coal. But as you have heard this morning, and particularly from Mr. Donovan, they are an inadequate alternative, in two respects. First, it is unclear what constitutes illegal monopolization under existing law, It is unclear whether an argument can be made that monopolization has occurred where a railroad operates on a track under a certificate granted to it by the Interstate Commerce Commission. Second, and in my mind, more importantly, is this question of relief. And let me give you a hypothetical.

Let us say that we have the San Juan coal fields in New Mexico and an electric utility in Texas, that desires to build and operate a coal fired electric generating facility. And assume that you have a proponent of a coal slurry pipeline that would like to move that coal for that shipper from New Mexico to the powerplant site in Texas and I can say such a project is under consideration. Third, let us assume that you have railroads that own rights of way and land and land rights between the power plant and the coal fields over which the pipeline must traverse. And fourth, let us assume that those railroads combine and say to each other, we are not going to let this entity cross this right of way, arguably committing an act of monopolization and a violation under section 1 of the Sherman Act, conspiracy.

Under existing law, the pipeline proponent, precluded from the market by the activities of the railroads would clearly have a remedy, there is no question, that the pipeline proponent would have standing and it could go into an antitrust court and say that we have been injured and it could recover the lost profits that it otherwise would have realized, had the illegal activity not occurred.

What about the shipper? The shipper as a customer in the market in question traditionally has standing under the antitrust laws. And under normal rules of the antitrust laws, one measure of damage for that shipper would be the illegal overcharge resulting from the act of precluding competition. But for a shipper on a class 1 railroad under exisitng antitrust laws and particularly in light of the second circuit opinion that Mr. Donovan discussed this morning, there is no such relief. The shipper while being in a position to argue illegal monopolization would not be in a position to recover damages. Would the damages be substantial? Sure they would be. San Antonio, TX is buying coal from the Powder River Basin today under a new contractual arrangement with a different set of railroads and next year will pay $9 per ton less because of the existence of competition than it paid last year. San Antonio for 10 years tried to get relief from the Congress and the Interstate Commerce Commission on its relationship with its railroad and was unable to. San Antonio next year will enjoy a 30 percent rate reduction because of the benefits of competition.

Take San Antonio as the Texas utility and apply that situation to the New Mexico market that I just talked about and under normal antitrust laws, the plaintiff/shipper in that case, would be able to use the overcharge, the $9 as the measure of damage. Under existing antitrust laws and the *Keogh* decision that Mr. Donovan referred to, the shipper is not allowed to.

I was disappointed to hear the testimony from the Department of Justice today that did not address the question of *Keogh*. It is my understanding that the Department of Justice has taken a position in various Federal circuit courts around the land that *Keogh* should no longer be the law. Apparently *Keogh* is the law, and if this committee addresses this antitrust question and addresses it seriously, I believe that this *Keogh* situation should be looked at and looked at very closely. There is no longer any rational basis for the existence of that doctrine.

I have no further statements, Mr. Chairman, but I would be happy to answer any questions.

Senator McConnell. Thank you, Mr. Palmer.

Mr. Feidler, do you have some questions?

Mr. Feidler. Yes, Mr. Chairman.

Senator McConnell. All right.

Mr. Feidler. Mr. Secretary, I believe that the Arizona Power Cooperative is a member of the NRECA. Could you comment on some of the problems that they are presently facing it in their relationship with railroads and how S. 447 might impact on those problems?

Mr. Bergland. Yes, fine. The Arizona Electric Power Cooperative (AEPCo) has a generating station at Cochise, AZ, and its coal supplies come 500 miles from Gallup, NM AEPCo has the dubious honor of paying the highest coal transportation rates in the West, 33 mils per ton mile. Its rate is $15.83 a ton, which is more than 300 percent of revenue-to-variable costs. By way of comparison, the Staggers Act set 180 percent of revenue-to-variable costs as the threshold of ICC review. AEPCo has appealed rate and the matter is now pending before the Commission.

Even if the cooperative could get other sources of coal, it could not transport that coal over the last portion of the haul by any carrier other than Southern Pacific. Accordingly AEPCo remains a captive to the Southern Pacific and pays freight rates which reflect that monopoly power.

This bill could theoretically provide a remedy by granting access to the tracks for the limited mileage covered by the Southern Pacific.

Mr. Feidler. Mr. Secretary, drawing on your background at the Department of Agriculture, could you comment generally on what impact you feel S. 447 would have for the agricultural industry of America?

Mr. Bergland. Well, we are seeing a complete change in the structure of agricultural marketing in the United States. Railroads were the principal mode of transport until interstate highways came into being some 40 years ago. In those early days, we saw elevators and other marketing terminals built about as far apart as a horse could haul a wagon in a day's drive, about 10 miles.

Now, of course, with modern transport, we found that most of those facilities were obsolete and we have been seeing a substantial reduction in marketing terminals over the past 50 years. Much of that is a natural process of evolution and is not damaging to the public interest. Recently, however, we have seen a phenomenon arise that does present a real threat, I think, to the competitive environment which is so important.

Large grain companies are entering into contractual arrangements with shippers to obtain some kind of an advantage in the marketplace. Now, no one knows what terms and conditions are set because those contracts are confidential. What we do know, though, is that grain companies are establishing what they describe as subterminal facilities, maybe 100 miles apart. They can load 52 cars at a time of one commodity headed for one destination. Obviously that is an advantage, but they enjoy an additional advantage in that they have a contract to haul that grain at a price which is different from the cooperatives and other independent marketing agencies competing in the surrounding area. As a result, those large organizations have an enormous competitive edge. Because of the advantage that they have in this secret deal with the railroads, they pay above the going price or offer more at the local market price than the competitors can. That is really cutting into the competition in the marketing structure for American agriculture, not only on the grains and bulk commodities which flow to the market place, but on the backhaul, and I think that there needs to be more light shed on these contractual arrangements. Clearly, there needs to be more competition than there is, if we are to see a competitive environment continue in both the marketing and distribution of farm supplies and products.

Mr. **Feidler**. Mr. Palmer, I would like to follow up with a quick question.

The Secretary, I think, was commenting also on the issue of abandonments. Could you comment generally on how you think that this bill would impact on abandonments?

Mr. **Palmer**. Yes, sir. We all know that one of the major problems that rural America has faced over the last few years, has been this question of line abandonments. In the more remote parts of the country, it has gone on with a vengence and people have been isolated and left without transportation service.

I believe that under this bill that the abandonment tendancy, the abandonment practices of the railroads would be slowed down if not stopped. And the reason that I say that is that under present procedures if a railroad abandons track, that track goes on the market. And if the track goes on the market, and you have an entrepreneur, somebody similar to the man who started MCI in the telecommunications business, to come in and form a new railroad company, you have new competition entering into the arena. I believe that the railroads when faced with the prospect of new competition, from new railroad companies would cease putting this track on the market and I believe that there definitely would be a beneficial impact on the parts of the country where isolated tracks have not yet been abandoned.

Mr. **Feidler**. Mr. Palmer, in your opening statement, you commented on the extra costs you felt that the present state of the law contributed to and which were passed on to the utilities and ultimately to the consumers.

Could you comment more fully on that? Also I think that you mentioned a study by Dr. Cooper from the National Consumer Federation. Could you comment on the results of that study?

Mr. **Palmer**. Yes, sir. The Dr. Cooper study did do an analysis of coal moving on class 1 railroads and as I stated, indicated in his judgment, an overcharge of approximately $1.3 billion over what would occur in a competitive market. The $1.3 billion represents extra revenues the class 1 railroads have enjoyed because of the absence of competition. At Western Fuels we have done some of our own studies and you have heard this morning that the Interstate Commerce Commission today has no jurisdiction to regulate a rate at all, unless that rate is perceived to be at a level of revenue to variable cost of 180 percent.

Our studies show that any rate in excess of a range of 150 to 160 percent of revenue to variable cost produces a monopoly return, and when I say a monopoly return, I have reference to a return that is in excess of a fair return on capital invested which is the normal benchmark for a competitive return.

In other words, the existing Interstate Commerce Act allows monopoly pricing. And that is another reason why we are here today and Mr. Dempsey is quite right, we are dissatisfied with that, because we are the people who are paying the monopoly return and we do not like it. We do not undertand why the law has to be the way that it is today to allow the vacuum that exists for people like Arizona Electric Power Cooperative to get relief from monopoly overcharges.

Mr. **Feidler**. Thank you, Mr. Chairman.

Senator **McConnell**. I want to thank all of the witnesses for appearing today. The hearing is concluded.

Mr. **Bergland**. Thank you, Mr. Chairman.

Mr. **Palmer**. Thank you, Mr. Chairman.

[Whereupon, at 11:45 a.m., the hearing was concluded.]

[Prepared statements of Bob Bergland and Fredrick D. Palmer follow:]

Testimony of

BOB BERGLAND
Executive Vice President

of the

NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

Mr. Chairman, my name is Bob Bergland. I am Executive Vice President of the National Rural Electric Cooperative Association (NRECA). NRECA is the national service organization of more than 1,000 consumer-owned, not-for-profit electric systems serving 25 million consumers in the more sparsely populated areas of 46 states.

I am pleased to be here today to support S.447,"The Railroad Antimonopoly Act of 1985", which offers the promise of equalizing the bargaining positions between coal users, such as electric utilities, and the railroads. S.447 would amend the Sherman Act by requiring a railroad with the only service in an area to permit other rail carriers, or shippers, to use its tracks where a monopoly exists. The bill further requires paying a reasonable price for use of those tracks to transport the shipper's commodity to the nearest competitive railroad or destination. Refusal by the owning railroad to permit the use of those tracks - or "essential facility" - would constitute a per se violation of the antitrust laws.

Specifically, the aim of this legislation is to aid captive shippers -- those who, because of the bulk of the commodity and the distances, must ship by rail, but are limited to a single carrier -- by substituting competition for the monopoly that presently exists.

NRECA's members and their consumer owners have been adversely affected by coal transportation costs and feel quite strongly about this issue. Coal is the major fuel source for generating the electricity that NRECA's own members produce. Of NRECA's approximately 1,000 members, some 62 are generation and transmission cooperatives which generate and/or transmit electrical power. As of January 1985, almost 78 percent of that generation was from coal and lignite for a total of 21,505 megawatts. Additional power is purchased by NRECA's members from outside generators (approximately 55%), much of which is coal-fired. Most (over 70%) of the coal-fired generating stations are "captive" to a single rail carrier.

Anything that affects the price of coal at the generating station affects our millions of users. While the price of coal has remained relatively stable for several years, the delivered cost of coal -- because of excessive railroad freight rates -- has continued to climb, raising the cost of electricity to our individual members. Transportation costs are, of course, directly passed through in the form of higher electric rates, and rural electric cooperatives already pay rates that are about 15% higher than that of competing utilities on a nationwide basis.

Because of the significance of rail transportation costs, the membership of NRECA at its 42rd Annual Meeting, held in February 1985 and attended by over 11,000 people, adopted the following resolution:

> Rail Transportation Tariffs
>
> The Congress has enacted the Staggers Railroad Act which substantially penalized captive shippers such as coal-burning electric utilities and grain producers. The Interstate Commerce Commission (ICC) has adopted the theory that railroads should be free to establish tariffs in excess of fully allocated costs for captive shippers as a means of compensating railroads for the movement of other commodities. As a result of this shift from the traditional ratemaking criteria, based upon actual cost of service, the electric consumers are being required to pay through electric rates for unjustifiable increases in the cost of transportation. These increases can cause present rail rates to double within five years.
>
> Our efforts to work with the appropriate coal transportation organizations, Congress and the ICC to reverse its punitive and unreasonable ratemaking philosophy have so far proved unsuccessful. We continue to believe that rates charged for the movement of coal should allow a reasonable rate of return to the railroads, based upon actual cost of service, but should not be allowed to become a means of subsidization of other railroad traffic.
>
> We encourage the ICC to recognize the captive nature of utility coal movements and to protect coal users against monopolistic pricing practices on the part of railroads.
>
> We urge Congress to recognize the serious nature of this problem and, further, we vigorously support legislative efforts to provide relief for shippers in a rail monopoly situation.

Due to the concern we have over these issues, NRECA has been active for many years in transportation issues. We were, of course, very involved in the legislative package which was developed in 1980 entitled "The Staggers Rail Act of 1980." This Act has substantially deregulated the rail industry, even though the package was considered to be a compromise that would balance rail and shipper interests. Unfortunately, the interpretation of that Act by the Interstate Commerce Commission (ICC) through its numerous rulemakings has resulted in upsetting the careful balancing of interests originally intended by Congress. While the ICC has pursued the goal of maximizing railroad revenues with a zeal that every profit-making business would envy, it has virtually ignored those provisions, such as the Long-Cannon Amendment, which Congress built into the Staggers Act in order to balance the interests of shippers and carriers. The bias of the Commission is illustrated most starkly by the Commission's proposal to limit rail rates on captive coal traffic only when the rate exceeds the cost to the shipper of building and operating its own railroad.

During the same time period that there has been a deterioration in regulatory protection for captive shippers, there has also been a dramatic increase in concentration of rail market power. Mergers between railroads have further reduced what little competition that was previously available, e.g., the creation of CSX and Norfolk Southern, the Union Pacific consolidation, Norfolk Southern's current efforts to buy Conrail, and rail carrier acquisitions of major intermodal competitors, such as CSX's purchase of American Commercial Lines. Ironically, the greater need for meaningful regulatory protections has arisen precisely at a time when the ICC has effectively been dismantling those same protections.

The bill before the Committee today would interject an element of competition into a monopoly market. It provides that a shipper or other railroad can have an alternative for the shipment of coal by using the tracks of the monopoly railroad. While our members do not necessarily want to be in the railroad business, they feel that they must bring their member consumers the most reasonably priced electricity possible, even if that means operating their own trains. When our members enter into negotiations with a rail carrier, there must be some alternative transportation to that provided by the single carrier. How can there be negotiation if there is not an alternative for resolving the problem of unfavorable rail rates? It should be noted that most rural electric generating systems own their own rail cars; thus, our members are already partly in the rail business, at the insistence, by the way, of the railroads themselves. If rail carriers cannot or will not provide reasonable service for reasonable fees, the opportunity should be given these shippers to complete the job already partially thrust on them by the railroads.

Mr. Chairman, S.447 will provide both competition and a yardstick by which to measure the true cost of providing rail service. By creating a competitive environment, increased efficiencies of service will be encouraged and competition will shape the marketplace. In my opinion, the granting of access to tracks is essential to real competition in the rail industry and a critical lever to encourage effective on-going bargaining between the rail carrier and the shipper.

The market ratemaking approach to rail rates embodied in S.447 has a great deal of merit. The ICC itself has argued strongly for such an approach, which relies heavily on negotiated rail rates. But a reliance on negotiated rates presumes that the shipper or electric utility has sufficient bargaining power to make negotiation meaningful.

Experience in recent years has shown that, in those instances where meaningful competition does exist, coal shippers have been able to negotiate satisfactory solutions to rate and service problems and incorporate those solutions into stable, long-term contractual arrangements. Such results, however, will remain the exception, rather than the rule, so long as matters remain unchanged.

The ICC's own recent captive shipper study, performed by Reebie Associates, demonstrates the value of an approach such as that embodied in S.447. According to the study, a coal-burning utility can obtain the benefits of modest competition if it can gain access to alternative rail service within 25 miles of the power plant. The study goes on to estimate that more than three-fourths of the coal-burning utilities in the United States could potentially be in this position -- if only they could reach the second railroad. The import of the study results is clear: a significant improvement in the existing situation with regard to competitive coal transportation service in many cases could be achieved if shippers could acquire trackage rights over as little as 25 or 30 miles of line.

Most of NRECA's members which have coal needs are also members of Western Fuels Association, Inc., and I will defer to Fred Palmer, who is on the panel with me today, for the specifics regarding their transportation problems. We do have other members, however, that are not represented by Western Fuels, and I would like to refer to a couple of them as examples of the monopoly abuses which exist for many electric utilities.

One of these involves Western Farmers Electric Cooperative, a generation and transmission cooperative from Anadarko, Oklahoma which obtains its coal by rail from Wyoming. The manager of Western, Tom Stevenson, accompanied me last year in my appearance before this committee. At that time, he related Western's experience in asking the Burlington Northern (BN) for trackage rights.

Western is currently buying coal from the Caballo Rojo mine just north of Coal Creek junction in Wyoming. The Chicago and Northwestern (CNW) has announced its intention to build track up to the first four mines north of Coal Creek junction, including that mine. The BN presently has a monopoly on all traffic originating north of Coal Creek junction. If the CNW is successful, that will provide at least one competitor to the BN's present monopoly for those mines. Shell's Buckskin mine, north of Gillette, will still be captive to the BN.

In anticipation of the CNW's access to the mine serving Western, the generating cooperative asked for a quote from the CNW and Union Pacific (UP) which could haul the coal for 1,210 miles to Durant, Oklahoma, within 67 miles of Western's Hugo generating unit near Fort Towson. They quoted $20.11/ton. For the last 67 miles, the BN currently has a destination monopoly and is demanding $13.42/ton, or more than 1/2 the rate that CNW/UP are charging for 1,219 miles. The BN, which currently provides rail transportation for the entire coal haul, is charging $23.69/ton or 17.5 mills/ton mile. From Durant to Fort Towson, it would be charging 227 mills/ton mile, or about 13 times as much.

Another of our member systems that finds itself subject to these monopoly abuses is Arizona Electric Power Cooperative (AEPCO), a generation and transmission cooperative located in Benson, Arizona. At present, its coal supplies come from Gallup, N.M. and it has the dubious honor of paying the highest coal transportation rates in the West: 33 mills/ton mile. Even if AEPCO could secure other sources of coal, it could not get that coal over the last portion of the haul by any carrier other than the Southern Pacific. Accordingly, it remains a captive to that railroad and pays transportation charges which reflect that monopoly power.

In both cases outlined here, S.447 could theoretically provide an effective remedy by granting access to the tracks for the limited mileage covered by the BN and the SP.

Finally, I would like to refer to an extensive and detailed study of railroad pricing, profits, etc. Dr. Mark Cooper, who conducted the study which was released about two weeks ago, estimates conservatively that more than $1.3 billion dollars per year in excess rail rates have resulted from the coal/utility market because of the ICC's failure to utilize the Staggers Act protections.

In conclusion, let me commend you for holding this hearing on S.447 which would do much to interject an element of competition into a monopoly market. The prices our members pay to move coal all too frequently reflect the lack of an alternative to the railroads' demands.

I appreciate this opportunity to present the views of NRECA, and urge the Committee to consider S.447 favorably.

NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION
1800 Massachusetts Avenue, N.W. Washington, D.C. 20036/202-857-9500

May 15, 1985

Honorable Strom Thurmond
Chairman, Senate Judiciary Committee
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Enclosed are the answers to the three questions submitted to me as a result of the Senate Judiciary Committee's April 23, 1985 hearing on S. 447, the Railroad Antimonopoly Act of 1985.

If you've further questions, please feel free to either call myself or Carolyn Herr Watts, a legislative representative on my staff, at (202) 857-9559.

Sincerely,

Bob Bergland
Executive Vice President

Enclosure

Question: You addressed the consolidation of 'country' elevators into new larger and regionally based elevators. Do the railroads serving these new elevators have an equity interest in them? If so, do you think this poses a threat to the grower with respect to the railroad's market power in terms of controlling grain prices at the grower level?

Answer: There is no known railroad with an equity interest in a country elevator, it is the confidential contracts large grain companies have with the railroads that makes the competition at the point of first sale unfair to a small country elevator.

Question: You indicate on page 7 of your statement that S. 447 could 'theoretically' provide an effective remedy to the captive shipper utility in Benson, AZ.

How do you envision the competitive access provisions of S. 447 working? Is the remedy contained in S. 447 "theoretical", or does Sec. 9(a)(1) provide AEPCO relief?

Answer: The reference to a "theoretical" impact on AEPCO was used in my testimony in order to avoid creating the false impression that AEPCO was presently in a position to unilaterally terminate its long-term coal supply agreement and move its coal source from Gallup, New Mexico. It plainly was not intended to imply that the benefit offered AEPCO by S. 447 is simply theoretical. To the contrary, Section 9(a) of the Bill would provide prompt, practical relief to AEPCO irrespective of the situation vis-a-vis its coal supply contract.

Presently, the only way to bring coal into Cochise (the site of AEPCO's generating station) is via the Southern Pacific. The nearest interchanges with other carriers are approximately 145 miles to the east (to the Santa Fe at Deming, New Mexico), and almost 500 miles to the west (to the Union Pacific at Colton, California). If S. 447 were enacted, and AEPCO were no longer bound by its current coal supply agreement, the provisions of Section 9(a) could be used to bring competitive service into Cochise via Colton or Deming, with competitive carriers (e.g., the Union Pacific) carrying the coal over the SP lines which would make up the last leg of the journey from any western origin. If, however, AEPCO remains tied to the Gallup origin -- as is presently the case -- S. 447 still would enable AEPCO to introduce an element of competition for its coal traffic. Section 9(a)(1) specifically provides that a shipper is entitled to require use of so much of the dominant railroad's facilities as is necessary "to connect with the track of a competing rail carrier or to reach the destination of shipment." Thus, if (as is the case with AEPCO) the nearest competing carrier is farther down the line from the origin than is the shipper's destination facility, S. 447 would permit the substitution of a new carrier over the entire route of movement.

Question: With respect to the AEPCO railrate, you mentioned the utility was being charged 323 mills/ton mile. What are the characteristics of this haul (length, distance, and grade), and what are the utility estimates of what constitutes a fair rate?

Answer: Arizona Electric Power Cooperative (AEPCO), headquartered in Benson, Arizona, hauls between 600,000 and 1 million tons of coal 500 miles from Gallup, New Mexico to the Apache Generating Station in Cochise, Arizona. AEPCO pays a rate of $15.83/ton which constitutes a rate of more than 330 percent of revenue-to-variable costs. For comparison, the Staggers Rail Act presumes a rate is reasonable until it reaches 180 percent of revenue-to-variable costs. (This revenue-to-variable costs ratio is the amount of revenue received by the railroad -- the rate charged -- as compared to the costs to the railroad excluding fixed costs.) AEPCO's rate is currently pending Interstate Commerce Commission review, but until any decision is made, the rate remains in effect and AEPCO must pay it. This $15.83/ton rate results in a charge of 32 mills/ton mile. This is the highest rail rate in the West. In addition to this haulage rate, AEPCO has purchased, at the request of the railroad, approximately 120 rail cars. Of this 500 mile haul, the first part consists of 356 miles carried by the Sante Fe railroad. The final section consists of 146 miles carried by the Southern Pacific railroad.

Arizona Electric Power Cooperative estimates that a "fair rate" would be somewhere between $8.50 and $9.50/ton.

It should also be noted that these 2 railroads have applied to the ICC for authority to merge; the application is presently pending.

TESTIMONY ON S. 447
OF

Fredrick D. Palmer
General Manager
Western Fuels Association, Inc.

MR. CHAIRMAN: I am pleased to be able to testify before this Committee today on a problem concerning those who depend on railroads to transport products they produce or purchase, and who are victims of monopoly practices in today's deregulated rail transportation marketplace.

My name is Fredrick D. Palmer. I am general manager of Western Fuels Association, Inc. We produce, buy and distribute coal. We are a cooperatively-owned fuel supplier to consumer-owned electric utilities including rural electric cooperatives and municipal utilities. We are a national organization with headquarters in Washington, D.C. Our 35 members' service areas extend into every state west of the Mississippi River, large areas of the southeast, and to Puerto Rico. A more detailed description is attached as an appendix to my testimony.

The question is asked of those of us who support passage of S. 447: isn't the Railroad Antimonopoly Act of 1985 a solution in search of a problem?

The answer is "no".

There is a problem. A large share of my time as general manager is spent finding means to solve the problem of monopoly practices by the railroads serving us. We have pursued antitrust litigation. We have devised business tactics to create competition where none exists. We are working for passage of this legislation.

As this committee is well aware, mergers have reduced to six the number of major national railroads. With the pending sale of Conrail, that number may be reduced to five. While these numbers, alone, suggest the potential for monopoly, the fact that in their service areas the major coal-hauling railroads generally provide the only transportation service available is all the more reason for Congress to take a closer look at the situation. The rail transportation market is inherently anti-competitive and it is becoming more so.

We commend the bill's sponsors for realizing there is a way to meet the needs of captive shippers and their customers to hold down freight rates in a deregulated business environment. The solution is simple: assure competition in the market. The principle is familiar; it is one on which American business traditionally is based.

Western Fuels is responsible for supplying fuel for nine different powerplants. In addition, we are responsible for the delivery of coal to each of those plants, except one. In discharging our responsibilities, we deal with five separate Class I railroads including:

- The Atchison, Topeka and Santa Fe Railway Company
- The Burlington Northern Railroad
- The Illinois Central Gulf Railroad Company
- The Missouri Pacific (now part of the Union Pacific System)
- The Union Pacific

Our experience teaches us there can be no question that much of the coal moved to powerplants over the nation's railroads is subject to monopoly power of the railroads involved. In most cases, a single carrier originates the move, or a single railroad serves a particular facility. Often, once a utility enters a long-term coal supply contract and sites its plant, it becomes a "captive shipper" subject to monopoly power by its sole source of transportation.

Since 1976, there have been parallel real price increases for the movement of coal on the nation's railroads, a phenomenon attributable to what economists call "price leadership", if not "price fixing".

The claim that railroads have been "responsible" in their pricing behavior with respect to coal is nonsense. The period 1974-78 represented the peak of new contract activity by utilities for steam coal, and western coal in particular. In 1985, you can buy coal on a long-term basis from Powder River Basin mines for less in nominal prices than you could ten years ago.

At the same time -- and from passage of the 4-R Act in 1976 when the railroads received new ratemaking freedoms -- rail rates for transporting coal have increased close to 40% in real terms.

Individual cases provide further evidence of monopoly power. Our studies show return on investment in a range of 55% to 575% for certain movements subject to ICC complaint proceedings. Our studies further show that any rate in excess of 150-160% of variable cost produces monopoly returns. Under the Staggers Act, the ICC lacks jurisdiction to even consider a rate until it reaches a 180% ratio of revenue to variable cost.

But, monopoly pricing is not the only way railroads exercise monopoly power to the detriment of the consumer.

Two of the five railroads we use provide marginal service.

Two of the five railroads hauling our coal have refused to quote junction rates where competition would be created for the remainder -- and majority -- of the movements.

One of the five railroads we work with has refused to provide a competitive quote from the junction to destination, even though it would represent a substantial portion of new business. In partial support of its refusal, the railroad cited certain unspecified complications that might arise in other dealings it has with its competition.

Two of the five railroads we move coal on refuse to discuss rate concessions and service obligations in return for a long term commitment by us.

Three of the five railroads with which we do business stand accused of an illegal conspiracy to block construction of a coal slurry pipeline that could have been a competitor for a portion of Western Fuels' business. The accusation has been made by the pipeline proponent in Federal District Court in Texas.

I submit to you that none of the incidents I cite from our business experience would have, nor could have, occurred in a competitive marketplace. Railroads are run by fine people. I consider many of them friends. But few of us would be able to refrain from exploiting monopoly power were it ours to use -- and railroad officials have proven this time and again.

Arguments over the reasonableness of rate levels dominate the railroad/shipper debate. These arguments are confusing and complicated -- and they are, in the main, irrelevant. The simplest way to determine rate "reasonableness" is to look at the rate level produced in a competitive environment.

Beginning in 1976, the City Public Service Board of San Antonio, Texas, attempted -- unsuccessfully -- to secure rail rate relief from the ICC and Congress. Over the years, they have watched their rail rates escalate from an intial quote of $7.90 per ton up to $27.67 per ton -- escalation of 350%. San Antonio undoubtedly spent over a million dollars in its attempts to convince the ICC, the courts, and Congress that it was being charged too much; but to no avail.

San Antonio's coal comes from a mine in Wyoming's Powder River Basin. That mine will shortly be served by two railroads instead of one. Over the past nine years of controversy, a single railroad has had access to that coal.

Given the new competitive environment, what has transpired? San Antonio was able to put the business up for bid between competitors. The successful carrier offered a bid of $18.78. Those $9.00 of rate relief will save San Antonio rate payers well over $500-million for the life of the coal contract. These dramatic savings are the result of one factor -- competition.

And the San Antonio experience is not unique.

Last year, Arkansas Power and Light had benefit of three-party competition for the movement of its Powder River Basin coal. Besides two railroads, Energy Transportation Systems, Inc. (widely known as ETSI), was still actively pursuing slurry pipeline service. Although the terms of AP&L's agreement with the successful bidder (a railroad) are confidential, there is no question that the economic benefits to AP&L were greater than those enjoyed by San Antonio and that the rate reduction approached the 30% reduction San Antonio achieved due to competition.

Recently, the Lower Colorado River Authority disclosed an interim short-term coal contract for its Powder River Basin hauls. Under a three-year agreement, Burlington Northern will ship coal at a rate of $22.00 per ton. That rate is a 17.6% reduction from LRCA's previous tariff rate of $26.70 for the same move, and on a short-term basis a competing railroad also got a piece of that business with a $22.35 per ton rate for a six-month period.

The benefits of competition are obvious.

The concept of S. 447 is straightforward in that regard. If railroads are to be deregulated, the existing market structure needs to be opened to provide for competition. The Railroad Antimonopoly Act accomplishes this by legislatively recognizing that railroad facilities are essential facilities where a railroad has bottleneck control over commerce.

Shippers are subject to antitrust law. Why should railroads be exempt if they act in ways which tend to restrain trade?

An argument can be made that carriers are already precluded from denying trackage rights with "an intent to monopolize" as set forth in S. 447. I'll accept that argument; but must note the legal standard has not yet been tested and it is far from certain that such an argument would prevail. A railroad defendant could be expected to argue that its monopoly is a "natural" one, conferred upon it by ICC certificate, and that the federal courts lack jurisdiction to order the use of such tracks by a competitor.

S. 447 will answer that argument and seal any conceivable loophole, denying contrary interpretation. It will also relieve shippers the necessity of litigation to prove the point.

Assuming that you could establish liability under existing laws, shippers have a further problem in the area of relief.

A plaintiff bringing an antitrust action does so with the expectation of recovering triple damages, attorney's fees, and costs. Whether such expectations are reasonable or not depends upon the strength of your case, not on the law.

While the law on relief for most potential plaintiffs is clear, it is not for shippers.

Railroads, under principles expounded by the U.S. Supreme

Court in Keogh v. Chicago Northwestern Railway Co., were granted antitrust immunity (implied immunity, technically, or at least a restriction on damages) because they were regulated by the Interstate Commerce Commission.

Keogh, the shipper, accused the railroads of price fixing, a conspiracy under Section 1 of the Sherman Act. Keogh had already lost a claim of excessive rates before the ICC, and the ICC had already found that the rate Keogh was challenging under the antitrust laws was the just and reasonable tariff rate.

In holding that Keogh could not maintain the antitrust suit, Justice Brandeis explained that Congress could not have intended that the ICC could determine that a tariff rate was lawful and reasonable and, at the same time, allow a shipper to have the rate struck down under the antitrust laws. Allowing antitrust damage, he reasoned, could result in a winning litigant paying an effective rate lower than the applicable tariff rate, creating a discrimination.

Keogh, for over half a century, has been the railroads' ultimate answer to antitrust suits.

In 1980, Congress virtually freed railroads from regulation with passage of the Staggers Act. The ICC has proven since then it is unwilling -- or is unable -- to enforce the limited shipper relief portions of the Staggers Act. I believe it can therefore be argued that the Keogh principle can no longer logically stand.

But Keogh has not been overturned and in some recent instances the decision has been relied upon in dismissal of antitrust actions against carriers. Keogh should no longer be the law. Under S. 447, it would not be.

Up to this point, my references have been based upon Western Fuels' experience as a captive shipper of coal. The benefits of S. 447 are not limited to coal shippers and utilities' alone. This trackage rights legislation directly benefits shippers of other bulk commodities. It covers fertilizer, ore, and perishable foods such as citrus fruits, and bulk commodities like wheat, corn, and soybeans. As such, it is important legislation for our beleagured rural economy.

Rural America has been hurt by a plethora of railroad line abandonments. A change in market structure as envisioned by this trackage rights legislation would decrease barriers to entry for new railroads through creation of new business opportunities. This holds forth the prospect of halting current abandonment practices.

Existing railroads would be acting against their own self-interest by continuing their abandonment policies where each abandoned track they place on the market could led to the birth of a railroad equivalent of MCI. In this way, railroad abandoment decisions could logically be expected to follow the dictates of the competitive market, too.

The cost of doing business in rural America is going up. The prices farmers receive for their produce and their markets are going the other direction. There has been a good deal of popular attention directed toward the crisis. You know better than anyone, solving the problem is incredibly complex. It defies simple solution.

S. 447 is a means by which several pieces of the mosaic can be addressed. Passage of S. 447 will not solve all of rural America's problems, but it can make an important contribution toward reducing the squeeze our fellow citizens feel. Western Fuels is sensitive to their needs. Our Board of Directors represents consumer-owned utilities who have as a goal of their service holding down costs. They are not in business to make profits to generate dividends for investors. Their owners are the people they serve. Passage of S. 447 will serve them well.

(end)

[Appendix]

DESCRIPTION OF WESTERN FUELS ASSOCIATION

Western Fuels Association, Inc., has as its primary mission the acquisition and delivery of coal to its members' electric generating stations. Western Fuels' membership consists of 35 consumer-owned utilities: rural electric cooperatives, municipal electrics, public power districts, and associations of municipal electrics.

In 1984, Western Fuels delivered over 11-million tons of coal to its members. This total includes purchases and mine production by Association subsidiaries. Revenues from coal supply services were $238-million during 1984. Among other operational expenses were $83-million in transportation charges, primarily for railroad deliveries. 1984 association operations realized approximately $1.5-million in margins for members.

The association's members' service areas extend from the Pacific Northwest to Florida; from Michigan to Arizona; and from a solid, 1600-mile stretch of the Canadian border to the Gulf of Mexico.

Twelve members received coal in 1984 through participation in Western Fuels; other members rely upon the Association for assistance in fuels and transportation planning.

Most of the coal Western Fuels delivers comes from mines in Wyoming's Powder River basin, but some comes from its own Brushy Creek and Deserado Mines (in southern Illinois and northwestern Colorado, respectively). The mines are operated by two wholly-owned subsidiaries, Western Fuels-Illinois and Western Fuels-Utah.

The association has contracted for delivery of 300-million tons of Wyoming coal to its members during the next ten to twenty-five years.

Western Fuels coal deliveries include:

-- The Missouri Basin Power Project's 1650-megaWatt Laramie River Station near Wheatland, Wyoming. Basin Electric Power Cooperative is project manager. Other participants include Tri-State Generation and Transmission Cooperative, Missouri Basin Municipal Power Agency, Heartland Consumers Power District, Lincoln Electric System (all of which are Western Fuels members), and two others.

-- Cajun Electric Power Cooperative's three-unit, 1620- mW Big Cajun No. 2, the first coal-fired electric generating facility in Louisiana.

-- The Kansas City, Kansas Board of Public Utilities' 240-mW Nearman Creek Station.

-- The Kansas City Board's Quindaro and Kaw Stations, which are older generating units receiving coal from the Brushy Creek Mine.

-- Sikeston, Missouri's 235-mW municipal power station.

-- Sunflower Electric Cooperative's 280-mW Holcomb Station near Garden City, Kansas.

-- Plains Electric Generation and Transmission Cooperative's 210-mW Escalante Station new Prewitt, New Mexico.

-- Short-term supplies have been provided for Virginia and Hibbing, Minnesota; the Southern Illinois Power Cooperative; Fremont, Nebraska Department of Utilities; and Associated Electric Cooperative.

Western Fuels is headquartered in Washington, D.C. Its Lakewood, Colorado, office is responsible for engineering and exploration. There are operations offices in Gillette, Wyoming; Alliance, Nebraska; and Prewitt, New Mexico. The Western Fuels-Illinois mining operations are near Galatia. Western Fuels-Utah offices are in Rangely, Colorado.

APPENDIX

Statement of
The Fertilizer Institute
In Support of S. 447
The Railroad Antimonopoly Act of 1985

The Fertilizer Institute * (TFI) submits this statement to the Senate Judiciary Committee in response to the April 23, 1985 Committee hearing on S. 447. TFI supports the concept embodied in the bill -- applying the antitrust laws to the railroad industry. Such action is the next logical step in the railroad deregulation process.

In the Bone Valley of Central Florida, the phosphate industry mines and processes 50-60 million tons a year of phosphate, an essential ingredient in fertilizer. Bone Valley deposits are 80 percent of the U.S. supply of, and one third of the world's demand for this irreplaceable component in our food chain. There are 21 phosphate rock mines and 11 mine owners in the Bone Valley but only one railroad -- the Seaboard System Railroad -- which serves the area with an average of 44 phosphate trains a day.

The Seaboard transports approximately 90 percent of all phosphate tonnage moving to Tampa Port where both origin and destination are served by rail and 98 percent of all phosphate tonnage originating in the Bone Valley to interior U.S. points.

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*TFI is a voluntary, non-profit association, whose members represent approximately 95 percent of the domestic fertilizer production in the United States. TFI's membership includes: producers, manufacturers, traders, retailer dealers and distributors of fertilizer materials. Its members are major shippers, receivers, and exporters of fertilizer and fertilizer materials and are a vital link in the nation's agriculture system.

Phosphate products rank second or third behind coal on the list of commodities which generate revenue for the Seaboard Railroad System -- in the neighborhood of $100,000,000.

The Port of Tampa handled 21,700,000 tons of phosphate products in 1983 which comprised 94.7 percent of its outbound tonnage -- enabling Tampa to rank ninth tonnage-wise in the nation.

The closest rail competition to the Bone Valley -- to the Seaboard System Railroad -- is 90 miles away, where the Norfolk Southern -- in competition with the Seaboard -- serves the Jacksonville, Florida area.

The Jacksonville Gateway to the Southern Railroad, was for years a competitive tool used by phosphate producers in negotiations with the Seaboard. However, shortly after the Staggers Act became law -- the Seaboard closed the Jacksonville gateway with the Southern thereby eliminating that rail competition. This action eliminated for phosphate producers, a competitive negotiation tool, and denied them the opportunity to enter into contracts with the Southern for phosphate tonnage originating out of the Bone Valley.

Such action is clearly in violation of the spirit of the antitrust laws but is permitted under the Interstate Commerce

Act (ICA). S. 447 addresses monopolized shipper situations described above and clarifies the application of the antitrust laws to the railroads and remedies available to shippers and to competing carriers for railroad antitrust abuses.

The Nation's antitrust laws were designed with one basic goal: the maintenance and preservation of competition in the marketplace.[1] This country's shippers of agricultural and farming products are especially sensitive to the importance of competitive alternatives for transportation services. These shippers are heavily dependent on the railroad industry for their transportation needs. Thus, the existence of as many alternate rail carriers as possible is essential if the Nation's agricultural and farm products are to move efficiently and economically. If America's agri-businesses lose competitive transportation alternatives, they will be forced either to pay higher rates or not move their products at all. The latter alternative is, of course, unacceptable; but if agricultural shippers must pay the higher rates, those costs either must be absorbed or passed on to the consuming public.

1/ See, generally United States v. Von's Grocery Co., 384 U.S. 270, 275 (1966); Northern Pacific R. Co. v. United States, 356 U.S. 1, 4 (1958); United States v. Aluminum Co. of America, 148 F. 2d 416, 427 (2d Cir. 1945).

Unfortunately, the last several years have seen a steady reduction of competition among rail carriers. Most obvious has been the string of ICC-approved mergers between some of the largest carriers. For example, the Atlantic Coast Line merged with the Seaboard Line to form the Seaboard Coast Line, the Seaboard and the Louisville & Nashville merged to form the Family Lines, the Baltimore & Ohio merged with the Chesapeake & Ohio to form the Chessie System, and the Chessie and Family Lines systems merged to form the CSX Corporation. Similarly, the Northern Pacific, the Great Northern and the Chicago, Burlington & Quincy merged to form the Burlington Northern, which then absorbed the Frisco. The Norfolk & Western and the Southern Railway are now merged into the Norfolk Southern, and the Missouri Pacific has been merged into the Union Pacific. Finally, the Santa Fe and the Southern Pacific presently are seeking Interstate Commerce Commission approval to merge. The trend is clearly towards regionalization of the Nation's railroads, with a single dominant carrier in each region. Indeed, many industry experts maintain that this day already has arrived.

Another significant anticompetitive trend has been taking place in the area of joint rates and reciprocal switching arrangements. Without going into excessive detail, joint rates and reciprocal switching arrangements are means by which railroads have eliminated competition. In regard to joint rates, suppose Railroad X offered single line service between points A and C, while Railroad Y only served point C but could connect with Railroad X at intermediate point B. Traditionally, Railroads X and Y would offer a joint rate between points A and C that would be competititve with Railroad X's single line rate and which would be lower than the combination of rates between points A and B and between points B and C:

_________Railroad X___________ B _ _ _ _ _ _Railroad Y _ _ _ _ _

A C

____

Railroad X

In regard to reciprocal switching, suppose a particular shipper's plant (P) is located on the tracks of a particular railroad (X). Railroads X and Y would negotiate reciprocal switching arrangements that permitted Railroad Y access to the plant:

_ _ _ _Railroad Y _

A + C

+

+ (+++ = Access to P via switching)

____

Railroad X

In turn, Railroad Y would permit similar access to Railroad X at another plant.

The result of joint rates and reciprocal switching arrangements provided competitive alternatives for the shipper, so that the shipper would not be limited to the use of the services of a single carrier. Unfortunately, beginning around 1982 and continuing to the present day, many of the Nation's largest rail carriers have been unilaterally -- and on a wholesale basis -- cancelling joint rates[2/] and cancelling or restricting reciprocal switching arrangements[3/] in those situations where the cancelling carrier can perform the service single line. Many agricultural shippers have been affected severely by these practices, as there are many routes where now only a single carrier can perform the single line service. Each cancellation, in turn, further decreases the number of routes where competition previously had been available. This has resulted in the growth of railroad monopoly power.

Many shippers have awakened to discover that suddenly they must deal with a monopoly carrier rather than carriers facing competition for their traffic. As expected, these monopoly carriers are

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2/ E.g., ICC Docket No. 39176, The Chlorine Institute, Inc. v. The Atchison Topeka & Santa Fe Ry. Co., et al.

3/ Id.

dictating the terms of the carrier/shipper relationship -- the shipper has no transportation alternative but to accept the railroad's terms.

Systematic railroad consolidation and wholesale cancellation or restriction of joint rates and reciprocal switching -- each harmful in its own way -- have combined to threaten a stranglehold on competition in the railroad industry. Ironically, this change in railroad practices has occurred at a time when deregulation largely has ended public utility style regulation of the surface transportation industry. Shippers no longer can expect to look to the Interstate Commerce Commission for protection against railroad monopoly activity.

Indeed, the present ICC has been instrumental in paving the way for much of the reduction in competition previously described. The Commission generally has favored the trend towards increased railroad consolidation. Moreover, the ICC thus far has refused to intercede against the cancellation of joint rates and reciprocal switching. In proceedings before the Commission's Suspension Board, the agency repeatedly has declined to investigate or suspend the relevant tariff publications and has denied a petition (supported by numerous shippers) to institute a general investigation of such practices.[4/] Moreover, a complaint filed with the ICC by the Chlorine Institute specifically challenging the cancellations and restrictions as unreasonable practices under the Interstate Commerce Act over a year ago has yet to be assigned for hearing.[5/] However, the Chlorine Institute and the Consolidated Rail Corporation have reached an agreement in this case (copy attached) that well-developed antitrust law principles should apply when evaluating the competitive effects of railroad activity.

In view of the ICC's handling of these and similar proceedings the agricultural community and other shippers are less than optimistic about the ICC properly exercising its authority to curb the unlawful growth of railroad monopoly power.

For all these reasons, the shipping public must now look to other forums in order to limit the growth of rail monopoly power. The obvious means is the application of the antitrust laws to the railroad industry. Indeed, in the absence of regulation, relief under the antitrust laws is essential if competition is to remain a factor in rail transportation.

[4/] Ex Parte No. 445, Standards for Intramodal Competition, served July 7, 1983.

[5/] ICC Docket No. 39176, The Chlorine Institute, Inc. v. The Atchison, Topeka & Santa Fe Ry. Co., et al..

However, the antitrust laws as presently structured do not provide a feasible mechanism for addressing the problems created by railroad consolidation coupled with joint rate and reciprocal switching cancellations and related actions. For example, Section 1 of the Sherman Act (15 U.S.C. 1), which outlaws conspiracies and combinations in restraint of trade, requires a showing of concerted action. The unilateral cancellation of a reciprocal switching agreement or a joint rate -- and no evidence of concerted cancellation activity has yet surfaced -- cannot violate Section 1. Section 2 of the Sherman Act (15 U.S.C. 2), on the other hand, does condemn unilateral monopolization and attempted monopolization. However, it would be exceedingly difficult for a shipper-plaintiff to define the relevant market in such a way as to establish either existing monopoly power or a substantial likelihood that monopoly power will be achieved.

It is for this reason that TFI supports the passage of S. 447. The bill would clarify that it is unlawful for a rail carrier, with intent to monopolize, to deny a shipper the use of tracks that afford sole access to the track of a competing railroad or the destination of the shipment.

Moreover, TFI notes that the bill is not a radical proposal. The concept of mandated access by competitors to the "essential facilities" of a monopolist has long been a part of antitrust law.

Indeed, the concept dates from the landmark Terminal Railway case.[6/] In that case, brought under Section 1 of the Sherman Act, the Government alleged that several railroads had conspired to control all terminal facilities in, and thus access to and from, St. Louis. The Supreme Court, finding both that such a conspiracy existed and that the cost of building and maintaining bridges made the creation of alternate access routes impractical, ordered that all railroads seeking access to St. Louis be granted reasonable access to the terminal facilities. Relying on Terminal Railways, the federal courts have applied the essential facilities doctrine in pure monopolization cases as well.[7/]

Further, there is no technical impediment to granting access to one railroad over the tracks of another railroad. In fact, this is sometimes done in merger cases, where Interstate Commerce Commission approval of the consolidation is conditioned on the grant of trackage rights over the consolidated system to carriers

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6/ United States v. Terminal Railway Association, 224 U.S. 382 (1911).

7/ E.g., MCI Communications Corp. v. AT&T Co., 708 F.2d 1081, 1132 (7th Cir.), cert. denied, -U.S.- (1983); Hecht v. Pro-Football, Inc. 570 F.2d 982, 992-93 (D.C. Cir. 1977), cert. denied, 436 U.S. 956 (1978); Mishawaka v. American Electric Power Co., 456 F. Supp. 1320, 1336 (N.D. Ind. 1979), aff'd. in relevant part 616 F.2d 976 (7th Cir. 1980), cert. denied 449 U.S. 1096 (1981).

outside the system, as a method of preserving competition. The grant of such trackage in merger and related cases has often been for hundreds of miles.[8] In the Southern Pacific-Santa Fe merger, numerous competing railroads are seeking significant trackage rights over the merged system, including the Union Pacific System, the Denver & Rio Grande Western R. Co., and the Missouri-Kansas-Texas R. Co.

While the ICC on occasion thus has been willing to impose trackage rights conditions, such provisions have not been automatic and generally have not been designed to eliminate railroad monopoly power. These ICC mandated trackage right thus have been ineffective in preserving competition. Moreover, the grant of limited trackage rights as a part of a merger proceeding will not protect the public against future anticompetitive activity.

8/ *E.g.*, *Union Pacific Corporation -- Control--Missouri Pacific Railroad Company*, 366 I.C.C. 459, 572-78 (1982), *appeal pending* (619 miles); *Chicago & N.W. Transp. Co.--Construction--Wyoming and Nebraska*, 303 I.C.C. 906 (1981), *aff'd.* No. 82-2341 (D.C. Cir. 1982) (76 miles); F.D. 29186, *Chicago, Milwaukee, St. Paul & Pacific R. Co. (Richard B. Olgilvie, Turstee)--Trackage Rights--Illinois and Indiana*, served January 24, 1980 (176 miles).

9/ ICC Finance Docket 30400, *Southern Pacific Santa Fe Corporation--Control--Southern Pacific Transportation Company* (still pending).

In summary, TFI strongly supports strengthening the application of the antitrust laws to deregulate railroads. Such legislation is absolutely essential if we are to continue the railroad deregulation process initiated with the 4R Act in 1976 and the Staggers Rail Act of 1980.

BEFORE THE

INTERSTATE COMMERCE COMMISSION

THE CHLORINE INSTITUTE, INC.,)
)
Complainant,)
)
v.) Docket No. 39176
)
THE ATCHISON, TOPEKA AND)
SANTA FE RAILWAY COMPANY, et al.,)
)
Defendants.)

MOTION OF THE CHLORINE INSTITUTE, INC. TO DISMISS COMPLAINT WITH RESPECT TO CONSOLIDATED RAIL CORPORATION WITH PREJUDICE AND FOR OTHER RELIEF

Paul M. Donovan
Gerald L. Richman
Stanley E. Hilton

LaRoe, Winn & Moerman
Suite 800
1120 G Street, N.W.
Washington, D.C. 20005
(202) 628-2788

Attorneys for The Chlorine Institute, Inc.

Dated: March 20, 1985

BEFORE THE

INTERSTATE COMMERCE COMMISSION

THE CHLORINE INSTITUTE, INC., Complainant, v. THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, et al., Defendants.	Docket No. 39176

MOTION OF THE CHLORINE INSTITUTE, INC. TO DISMISS COMPLAINT WITH RESPECT TO CONSOLIDATED RAIL CORPORATION WITH PREJUDICE AND FOR OTHER RELIEF

The Chlorine Institute, Inc. (the "Institute"), complainant herein, and Consolidated Rail Corporation ("Conrail"), one of the defendants, have executed a Settlement Agreement, dated March 19, 1985 and attached hereto as Appendix A, designed to resolve all disputes between these two parties in the above-captioned proceeding.

Under that Agreement, the Institute and Conrail agree that in all future cases before this Commission between the Institute and Conrail concerning (a) cancellation of joint rates and/or through routes and (b) establishment of through routes, joint rates and reciprocal switching (including the level of compensation for reciprocal switching), the Institute and Conrail will raise no claims or defenses not cognizable under the standards set forth in Exhibit 1 of the Agreement.

The standards in question would apply antitrust law principles to evaluate the competitive effects of challenged railroad actions. The Commission has long looked to such principles for guidance in evaluating claims that railroad actions are anticompetitive, and the Institute and Conrail believe that challenges the Institute might bring against Conrail in the future concerning the enumerated joint rate, through route and reciprocal switching issues should be resolved under the Interstate Commerce Act on the basis of those principles. For this reason the Institute has agreed, in consideration of Conrail's agreement to the enumerated standards, to move to dismiss the complaint with respect to Conrail with prejudice. The Institute seeks such dismissal with this pleading.

The Institute recognizes that the Settlement Agreement binds only the Institute and Conrail and resolves the dispute in Docket No. 39176 only with respect to the Institute and Conrail. However, the Institute submits that the agreed standards, if adopted by this Commission as interpretative rules or a general statement of policy, would resolve all substantive issues raised by the instant complaint. Were the Commission thus to issue an order adopting these standards as standards under the Interstate Commerce Act for application in all Commission proceedings concerning (a) cancellation of joint rates and/or through routes and (b) establishment of through routes, joint rates and reciprocal switching (including the level of compensation for reciprocal switching), the Institute would move for dismissal of the entire complaint in Docket No. 39176.*/

WHEREFORE, The Chlorine Institute, Inc. hereby moves this Commission to serve an order dismissing the complaint in this proceeding with respect to Consolidated Rail Corporation with prejudice.

FURTHER, The Chlorine Institute, Inc. hereby moves this Commission to serve an order adopting the standards enumerated in Exhibit 1 to the attached Settlement Agreement as standards under the Interstate Commerce Act for application in all Commission proceedings concerning (a) cancellation of joint rates and/or through routes and (b) establishment of through routes, joint rates and reciprocal switching (including the level of compensation for reciprocal switching).

Respectfully submitted,

Gerald L. Richman

Paul M. Donovan
Gerald L. Richman
Stanley E. Hilton

LaRoe, Winn & Moerman
Suite 800
1120 G Street, NW
Washington, DC 20005
(202) 628-2788

Attorneys for The Chlorine
Institute, Inc.

Dated: March 20, 1985

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*/ The Institute's motion to dismiss the complaint with respect to Conrail is not made contingent upon such an order by the Commission.

APPENDIX A

BEFORE THE

INTERSTATE COMMERCE COMMISSION

THE CHLORINE INSTITUTE, INC., Complainant,	)	
v.	)	Docket No. 39176
THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, et al., Defendants.	)	

SETTLEMENT AGREEMENT BETWEEN THE CHLORINE INSTITUTE, INC. AND CONSOLIDATED RAIL CORPORATION

WHEREAS the complaint in this proceeding, brought by The Chlorine Institute, Inc. (hereinafter the "Institute") representing the interests of its members, alleges that certain defendants, including Consolidated Rail Corporation (hereafter "Conrail"), cancelled certain joint rates and routes and restricted reciprocal switching arrangements and agreements, for the purpose or with the effect of reducing competition; and

WHEREAS the Institute acknowledges that Conrail denies the allegations contained in the complaint; and

WHEREAS the Institute and Conrail believe that the Interstate Commerce Commission should employ well-developed antitrust law principles when evaluating the competitive effects of railroad activity; and

WHEREAS the Institute and Conrail are desirous of achieving workable standards for resolving future competitive access disputes between the Institute and Conrail;

NOW THEREFORE in consideration of the premises, covenants and considerations set out herein, the Institute and Conrail agree as follows:

1. The Institute and Conrail agree that, in all future cases before this Commission between the Institute and Conrail concerning (a) cancellation of joint rates or through routes or (b) establishment of through routes, joint rates or reciprocal switching (including the level of compensation for reciprocal switching), the Institute and Conrail will raise no claims or defenses not cognizable under the standards set forth in Exhibit 1 hereto.

2. In consideration of the agreement described in Paragraph 1, the Institute will move promptly to dismiss with prejudice its complaint in Docket No. 39176 with respect to Conrail. The Institute and Conrail agree that with such dismissal the Institute waives all rights to challenge in any forum the past practices of Conrail cited by the Institute in this proceeding.

3. Subject to the dismissal described in Paragraph 2, the Institute and Conrail waive all right of judicial review

(direct, collateral, or otherwise) of the standards set forth in Exhibit 1 hereto and waive all right to base claims or defenses on any standards other than those contained in Exhibit 1 hereto.

3. This Settlement Agreement shall inure to the benefit of and be binding upon the heirs, administrators, executors, successors and assigns of the parties hereto.

By:
Paul M. Donovan
Gerald L. Richman
Stanley E. Hilton
LaRoe, Winn & Moerman
1120 G Street, N.W.
Washington, D.C. 20005
(202) 628-2788

Attorneys for The Chlorine Institute, Inc.

Dated: March 19, 1985

By:
Paul A. Cunningham
Robert M. Jenkins, III
Pepper, Hamilton & Scheetz
1777 F Street, N.W.
Washington, D.C. 20006
(202) 842-8100

Attorneys for Consolidated Rail Corporation

Dated: March 18, 1985

EXHIBIT 1

1. Cancellations of Joint Rates and/or Through Routes.

(a) The Commission shall determine that a cancellation of a joint rate or a through route is not consistent with the public interest under 49 U.S.C. 10705(e) if it finds that the cancellation, and any rate that would remain in place after the cancellation, constitute:

(i) a contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations; or

(ii) monopolization, or attempt to monopolize, or combination or conspiracy with any other person or persons, to monopolize any part of the trade or commerce among the several States or with foreign nations.

In making its determination, the Commission shall take into account all relevant factors. Any investigations under the terms of this paragraph will be conducted and concluded by the Commission on an expedited basis.

(b) The cancellation of a through route or joint rate shall be presumed to violate the standards of paragraph 1(a)(i) or (ii) if the complainant demonstrates that the route at issue is of reasonably comparable or superior efficiency to any competitive single line route of the cancelling carrier and that the rates of the cancelling carrier will foreclose effective competition over the route at issue. The cancelling carrier may rebut the presumption by a showing that the cancellation or subsequently applicable rates will not eliminate effective competition for the traffic at issue.

2. Establishment of Through Routes, Joint Rates and Reciprocal Switching.

A through route or joint rate shall be prescribed under 49 U.S.C. 10705(a) or reciprocal switching or compensation therefor shall be established under 49 U.S.C. 11103(c) if the Commission determines that the prescription or establishment is necessary to remedy or prevent an act which constitutes:

(i) a contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations; or

(ii) monopolization, or attempt to monopolize, or combination or conspiracy with any other person or persons, to monopolize any part of the trade or commerce among the several States or with foreign nations.

In making its determination, the Commission shall take into account all relevant factors. Any proceedings under the terms of this paragraph will be conducted and concluded by the Commission on an expedited basis.

3. Effect of Commission Determinations or Findings Under The Standards Set Forth in This Agreement.

Any Commission determinations or findings under the preceding paragraphs with respect to compliance or non-compliance with the standards of paragraph 1(a)(i) or (ii) or paragraph 2(i) or (ii) shall not be offered in evidence or otherwise introduced in, or given any res judicata, collateral estoppel or other effect in, any litigation involving the same facts or controversy arising under the antitrust laws of the United States.

Certificate of Service

I hereby certify that copies of the foregoing Motion and attached Settlement Agreement have been served this day on all parties of record in this proceeding by first-class mail, postage prepaid.

Gerald L. Richman

Dated: March 20, 1985

OFFICE OF THE GOVERNOR
STATE CAPITOL
AUSTIN, TEXAS 78711

MARK WHITE
GOVERNOR

May 3, 1985

The Honorable Strom Thurmond
Chairman, Committee on the Judiciary
Dirksen Senate Office Building
Room 224
Washington, D.C. 20510

Dear Senator Thurmond:

On behalf of the State of Texas, I appreciate the opportunity to file comments in support of S. 447, the Railroad Antimonopoly Act of 1985. I applaud your efforts to bring this issue before the members of the Senate Judiciary Committee as another approach for captive shipper relief. I request inclusion of these remarks in your official record.

Yours truly,

Mark

Mark White
Governor of Texas

STATEMENT OF THE HONORABLE MARK WHITE
GOVERNOR OF THE STATE OF TEXAS
FOR THE SENATE COMMITTEE ON THE JUDICIARY

April 29, 1985

In the State of Texas, coal shipments are virtually 100 percent captive, with 86 percent of the 25.4 million tons of coal coming into the state in 1983 controlled by a single railroad. I call that a monopoly. During that same year, railroad transportation charges represented approximately 60 percent of the price of coal delivered to electric utilities in the state.

In 1985 I am happy to say that is changing. In March I was able to announce a contract between Utility Fuels Inc. and Burlington Northern - Atchison Topeka and Santa Fe Railroads that would transport coal from the Powder River Basin at a savings to Houston Lighting and Power customers of more than $60 million a year for each of the next 15 years. Later that month a 20-year contract between Chicago and North Western and the City Public Service Board of San Antonio was signed that dropped the transportation price of coal from $27.67 per ton to $19.56 per ton. An almost 30% reduction! With our long history of attempts to secure rate relief, why are we suddenly so successful? The answer is competition, the willingness of a rail carrier to reach into the highly profitable geographic domain of another, and allow the market place to determine prices.

I wish it were possible for all captive shippers to achieve this goal, but unfortunately, not every railroad can afford to make that kind of investment. We must work harder then, to create an atmosphere of competition for those shippers who have no access to competition.

One method for assuring competition is proposed by the Railroad Antimonopoly Act of 1985. It adds a new section to the Sherman Act prohibiting a carrier with monopoly service from denying a shipper the use of the carrier's track. This bill attempts to clarify the current confusion over the railroad's inclusion or exemption from antitrust law; it fills the void between the Sherman and the Staggers Act.

I have long been an advocate for a national transportation system that meets and balances the needs and interest of rail carriers, their users and the public. As Attorney General I was involved in deliberations that led to enactment of the Staggers Rail Act in 1980. Since then, the ICC has proven that it is either unwilling or unable to enforce the limited shipper relief portions of the Staggers Act. I have also endorsed S. 477, the Consumers Rail Equity Act of 1985, with its efforts to tighten procedures at the ICC. Either or both legislative approaches would improve the captive shippers' access to competition.

For these reasons, I am endorsing S. 447, the Railroad Antimonopoly Act of 1985, as a call to protect shippers and consumers subject to railroad monopoly power.

THOMAS R. KUHN, Executive Vice President

EDISON ELECTRIC INSTITUTE The association of electric companies

1111 19th Street, N.W.
Washington, D.C. 20036-3691
Tel. (202) 828-7400

May 7, 1985

Honorable Strom Thurmond
Chairman
Judiciary Committee
United States Senate
218 Russell Building
Washington, D.C. 20510

Dear Mr. Chairman:

I appreciate the opportunity to submit comments regarding S. 447, the Railroad Antimonopoly Act, on behalf of the Edison Electric Institute (EEI). EEI is the national association of the investor-owned electric utility industry. Its member companies provide 75% of all electric power purchased in the United States and serve approximately 73% of all domestic consumers of electricity.

EEI appreciates your Committee's recognition of the importance of reasonable rail rates for captive traffic to consumers of electricity and other products. We look forward to continuing to work with you on this issue of considerable economic importance to consumers throughout the nation.

Sincerely,

Tom Kuhn

Thomas R. Kuhn

Enclosure
TRK:llj

May 7, 1985

STATEMENT OF THE EDISON ELECTRIC INSTITUTE

Before the Senate Committee on the Judiciary

Regarding S. 447

The Edison Electric Institute (EEI) is pleased to submit comments regarding S. 447. EEI is the national association of the investor-owned electric utility industry. Its member companies provide 75 percent of all electric power purchased in the United States and serve approximately 73 percent of all domestic consumers of electricity. EEI submits this statement on behalf of its member companies and their customers.

Electric utilities paid railroads approximately $5.5 billion in 1984 alone to transport coal. On a national basis, railroad freight rates represent a substantial portion of the delivered price of coal, in some cases as high as 80 percent. Consumers of electricity pay for these transportation costs in their electricity rates. As noted by the National Association of Regulatory Utility Commissioners in a background paper dated April 10, 1985:

> "In every jurisdiction, annual rail transportation charges are recovered dollar-for-dollar from utility ratepayers as an expense item, in some cases through a fuel adjustment clause. Transportation costs are not a rate base item upon which a utility earns its profit."

It is therefore essential to electric utilities and to our customers - your constituents - that the rates for transporting coal to captive shippers be fair and reasonable.

EEI is pleased that Senator DeConcini and his colleagues have recognized the importance to consumers of electricity - and of other products - of reasonable rail rates for captive traffic and of the need to provide reliable and effective means to achieve this goal. Your active interest in addressing this consumer issue, as evidenced by this hearing on S. 447, significantly furthers our industry's efforts to obtain reasonable coal rail transportation rates. EEI and our member companies sincerely appreciate your continued interest in the problem of captive rail shippers.

Although EEI and its member companies share with Senator DeConcini and his colleagues the common desire to assure the reasonableness of rates for captive rail shippers, we have not taken a position on this particular bill. Nevertheless, we provide the following comments to assist the Committee in its deliberations.

During 1984, electric utilities used coal to produce over 56 percent of the electricity generated in this nation. This required the use of over 600 million tons of coal - 85 percent of domestic coal consumption. By 1990, utilities estimate that they will require 750 million tons of coal annually to generate electricity. Almost 50 percent of coal powered utility plants are totally dependent upon railroads for the delivery of coal. Over 90 percent of these plants receiving their coal by railroad are captive to a single railroad, and have no practical alternative means of coal transportation.

During congressional debate and deliberations leading up to the passage of the Staggers Rail Act of 1980, Congress concluded that many shippers, particularly coal shippers, are captive to individual railroads and have no realistic transportation alternative. To protect such shippers, the Congress, through the Staggers Rail Act, continued the requirement for the Interstate Commerce Commission (ICC) to regulate rail rates for captive traffic while it deregulated rail rates for competitive traffic.

The Court of Appeals for the District of Columbia Circuit has recognized the dual purposes of the Staggers Act. In a decision repudiating the Commission's deregulation of export coal rates, it stated:

> [T]he underlying approach of the [Staggers Act] was to move toward much greater reliance on market forces rather than regulation to govern rail carriage, but to temper that move with a policy of retaining regulation where the market would be insufficient to protect shippers and the public from abusive railroad practices.

Coal Exporters Ass'n v. United States, 745 F.2d 76, 81 (D.C. Cir. 1984).

Notwithstanding the Staggers Act's goal of promoting competition, shippers are increasingly faced with fewer and fewer railroad competitors due to mergers and acquisitions over the past several years. For example, if the pending combination of the Norfolk Southern and Conrail is approved, 3 major railroad systems will handle over 80 percent of all coal traffic in the nation and over two-thirds of the coal delivered to captive power plants. Concurrently, the railroads have also successfully forestalled significant competitive alternatives, such as coal slurry pipelines, and have begun to take over barge lines, which have traditionally served as major competition to railroads in the transport of bulk commodities.

These trends suggest that when the railroads point to the success of the Staggers Act in promoting competition, they are not referring to competition for bulk commodities. Their own actions have maintained, if not increased, the pool of captive shippers which remain dependent upon the rate protections offered by the Staggers Act.

Even for captive traffic, however, the Staggers Act allowed the railroads considerable rate-making flexibility. As of October 1, 1984, the Commission's jurisdiction extended only to rates exceeding 180% of the variable cost of the transportation to which that rate applies. In contrast, the railroads would be revenue adequate if they received an average revenue/variable cost ratio of 150% to 155% on all their traffic.

By establishing an ICC rate jurisdictional threshold at 180% of variable cost and other measures, the Staggers Act already provides railroads considerable flexibility to engage in differential pricing. But once rates exceed the statutory thresholds, the ICC must assure that a railroad does not abuse its monopoly control to impose unreasonably high rates on captive traffic. 49 U.S.C. § 10701a.

In making this determination, the ICC must consider the additional revenues a railroad could be earning on all of its competitive traffic (49 U.S.C. § 10707a(e)(2)(B) and (C)), the revenue adequacy status of the carrier, and whether the carrier is being operated under "honest, economic and efficient management." 49 U.S.C. § 10704.

Despite the limited scope of its responsibility over rail rates, the ICC has virtually abdicated any attempt to protect the captive shipper. Significantly, the ICC has never found a railroad rate to be unreasonably high under its post-Staggers standards. Instead, the ICC, through a series of rulemakings, allows the railroads to exercise virtually unrestrained monopoly power over the captive coal rates within its jurisdiction.

For example, the ICC's proposed "Maximum Coal Rates, Nationwide," effectively endorses monopoly pricing as the economic basis for regulating rates to captive shippers. The primary "constraint" which the ICC would impose upon rail rates - the stand-alone cost - is the price at which a shipper theoretically could construct its own railroad as an alternative to its monopoly rail service. This has nothing to do with what constitutes a maximum "reasonable" price because the cost to the prospective purchaser of replacing a product or service could be many times higher than the price at which the monopolist would earn a fair profit. The National Association of Regulatory Utility Commissioners (NARUC) has criticized this proposal, stating:

> We fail to see . . . how stand-alone costs can constitute a "competitive standard" in a market for which (by definition) there is no competition; rather, stand-alone costs merely reflect the maximum level at which a monopolist (in the absence of regulation) could price its product or service. Viewed in this way, this so-called "constraint" could never be attributed to ICC regulation, but rather would operate without any regulatory intervention.
>
> [T]he Commission's "stand-alone" constraint is but a smokescreen, which at best may have limited theoretical value, but has little impact upon the monopoly power of market dominant railroads. Comments of the National Association of Regulatory Utility Commissioners, Ex Parte No. 347 (Sub-No. 1), July 28, 1983, pp. 7-8.

Neither this "constraint," nor the others the ICC proposes to adopt, establish a basis for determining a maximum reasonable rate.

In other critical proceedings to implement the Staggers Rail Act, the ICC also has ignored the intent of Congress. Since 1981, the ICC has decided repeatedly that all major railroads in this country are not earning "adequate revenues." It has made this determination the centerpiece of its other actions which are designed to provide the railroads with unrestrained pricing capability. The methodology developed by the ICC to assess the financial health of a railroad seriously overestimates railroad expenses and underestimates revenues. The overall effect of the entire revenue adequacy process is to make all railroads appear to be in relatively poor financial health. Moreover, the ICC acknowledged more than two years ago that the data it relies upon to calculate a key element in the revenue adequacy determination - railroad return on investment (ROI) - contain "anomalies" which "affect the ROI to a material degree." Ex Parte No. 393 (Sub-No. 1), served March 9, 1983, Decision, p. 3. Nevertheless, the ICC has not yet cured this problem.

The myth that all railroads are still suffering from the "Penn-Central syndrome" must be dispelled. This myth appears to be based in large part upon projections of railroad performance (excluding Conrail) which the Department of Transportation (DOT) prepared in 1978 and which projected that the railroads would experience a $21.6 billion capital shortfall between 1976 and 1985. However, actual railroad operations have been far more favorable than DOT's earlier projections. Based upon actual experience through 1984 and reasonable projections for 1985, it now appears that these railroads will experience a $10.5 billion capital surplus during this same period.

The myth of the Penn-Central syndrome is most significantly contradicted by the fact that the Norfolk Southern Corporation has been chosen by DOT over several other financially healthy non-rail firms as the successful bidder for Conrail. Norfolk Southern, which bid $1.2 billion for Conrail, obtained at least 87 percent of its 1984 net income from railroad operations which the ICC consistently has found to be "revenue inadequate." The ICC's characterization is clearly inconsistent with Secretary of Transportation Dole's February 8, 1985 claim that Norfolk Southern is "highly profitable."

The following statements demonstrate the vast disparity between the actual financial health of the railroads and the Commission's determinations that they are "revenue inadequate:"

> "Earnings for the U.S. freight railroads' operation increased by a spectacular 120 percent. Net income of $2.7 billion exceeded 1983 earnings by $1.5 billion."
>
> Mary DeSapio, "Wall Street Viewpoint,"
> Modern Railroads, April 1985
>
> "CSX common stock has out-performed the average of its peer group of transportation and natural resource companies and the average of the Standard & Poor's 500 Index."
>
> CSX Corporation
> 1984 Annual Report
>
> " . . . in 1984 Norfolk Southern delivered record earnings, while moving toward its goal of becoming a total transportation company . . . . It was a year of growth in revenues and income, as well as a year which marked major proposals for expanded rail coverage and corporate diversification."
>
> Norfolk Southern Corporation
> 1984 Annual Report

EEI and representatives of our industry have repeatedly testified that we are alert and sensitive to the need for a vital and vigorous rail industry capable of meeting our expanding requirements for delivering our most abundant energy source. We recognize the need for adequate revenues on coal traffic, but, at the same time, believe that railroad revenue adequacy should be determined fairly in a manner consistent with approaches applied to other industries. In addition, we believe that the Interstate Commerce Commission should act as Congress intended and balance the need for adequate revenues with the obligation to maintain reasonable rates where there is an absence of effective competition.

It is important to emphasize that coal already contributes a sizeable share to railroad operating profits. Nationally, coal contributes the most tonnage, revenue and profit to the railroad of any commodity. Of these criteria, profit is obviously the most significant to consider - and the one the railroads are least likely to discuss. Coal is considerably more profitable than other traffic. The latest available ICC data indicates that in 1981, coal contributed $2.6 billion to total railroad gross operating profit. This represents over one third of the railroad's gross operating profit in that year. Coal transported for both captive and competitive shippers yields a 44 percent margin over cost while the average of all traffic is only 26 percent. Among the reasons for coal's profitability is the fact that it is increasingly being carried in extremely efficient unit trains and utility shippers are providing more equipment, thereby reducing the railroads' costs. Utilities currently own in excess of 33,000 coal cars, a 10 fold increase in the last 10 years, with an estimated value exceeding $1.25 billion. Over 40 percent of rail coal moves in utility-owned cars. In addition, utilities have made substantial investments in terminal facilities.

EEI and its member companies have repeatedly contested the Commission's unfair and distorted application of the Staggers Act and have challenged Commission decisions in the Courts. We have, as of yet, received no relief from the Commission. As time has passed, and as the pattern of the Commission's abdication of its responsibilities has become more obvious, some courts have begun to disagree with the Commission's decisions and criticize it for failing to implement the intent of the Staggers Act. See e.g., Arizona Public Service Company v. United States, 742 F.2d 644 (D.C. Cir. 1984). However, courts often defer to the expertise of the Commission, particularly when confronted with costing, accounting and/or financial issues such as the proper standards for revenue adequacy, Bessemer & Lake Erie R.R. Co. v. ICC, 691 F.2d 1104 (3rd Cr. 1982), or rate reasonableness, Potomac Electric Power Co. v. ICC, 744 F.2d 185 (D.C. Cir. 1984); Wheeling - Pittsburgh Steel Corp. v. ICC, 723 F.2d 346 (3rd Cir. 1983).

No matter what their result, efforts to contest the ICC's decisions in the courts are extremely time-consuming and burdensome. While they take place, consumers are being increasingly burdened with the costs of unfair and unwarranted rail rates.

Action by Congress offers the only timely and effective solution. Unless the Congress addresses this consumer issue, the stage has been prepared for the unjustified transfer of billions of dollars from the pockets of the beleaguered consumers to the coffers of the prospering railroads. EEI therefore commends your interest in these problems of considerable economic impact to consumers throughout the nation. We look forward to continuing to work with you toward a legislative solution.

FEDERAL TRADE COMMISSION
WASHINGTON D.C. 20580

OFFICE OF
THE CHAIRMAN

May 15, 1985

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for requesting the view of the Federal Trade Commission concerning S.447, the "Railroad Antimonopoly Act of 1985." This proposed legislation would amend the Sherman Act to prohibit railroads from denying usage of their track and other facilities to shippers of certain commodities and would apply Clayton Act penalties to violations of the legislation's provisions.

The Federal Trade Commission opposes the proposed legislation. The legislation deals with an issue that is addressed by existing law. It appears to be inconsistent with broadly accepted approaches to enforcement of the antitrust laws. It would be administratively inefficient. Finally, it would very probably have significant adverse effects on the rail transportation system.

Portions of the Interstate Commerce Act already deal with access to rail facilities by competing railroads.[1] Indeed, the Interstate Commerce Commission, the agency charged with railroad rate regulation, has just initiated two proceedings dealing with market dominance and intramodal rail competition that address directly the issues raised in the proposed legislation.[2] We believe it would be a more efficient use of government resources to rely upon the ICC process for evaluating allegations of market dominance and, where shippers have problems with that process, to encourage them to seek to influence the way in which it is administered, rather than to add another process that will enmesh the judiciary in the daily operations of our nation's railroads. Moreover, even absent this pervasive regulatory scheme, current antitrust law is sufficient. The Supreme Court has held that, under certain circumstances, a monopolist who controls an "essential facility" must permit access on reasonable terms to competitors.[3]

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[1] *See e.g.* 49 U.S.C. §11103.

[2] Interstate Commerce Commission, Ex Parte No. 320 (Sub-No. 3), *Product and Geographic Competition* (March 26, 1985); Ex Parte No. 445 (Sub-No. 1), *Intramodal Rail Competition* (March 22, 1985).

As a general matter, it is highly inappropriate to amend the antitrust laws with industry-specific price control regulation. The antitrust laws are of general applicability and they represent an effective yet flexible mechanism for preventing anticompetitive behavior on a case-by-case basis. More specifically, antitrust enforcement traditionally requires a two-step approach to determining whether a particular practice has or is likely to have anticompetitive effects: (1) a definition of the relevant market in terms of all possible constraints on the exercise of market power; and (2) a determination of whether or not effective competition is present in that market and whether the practices at issue threaten competition in that market. This bill would eliminate those steps by defining the market in advance as a rail route or facility over which a carrier has exclusive control, and by establishing the presumption that exclusive control of such a route or facility confers monopoly power on the railroad.

The difficulty with this approach is that the process of defining relevant markets in antitrust cases often reveals many sources of effective competition. There is no reason to believe that railroad markets would provide an exception. Constraints on the exercise of market power by railroads could arise from competition from other modes, such as motor vehicles or water carriers. The existence of alternative sources of or substitutes for the commodity involved may also substantially constrain the railroads' exercise of market power. The fact that only one railroad serves a specific line segment, therefore, is not proof that it possesses sufficient market power to set monopoly rates.

In addition, by creating an antitrust offense regardless of the anticompetitive effects of the practice in question, the bill seems to contravene the trend of recent Supreme Court interpretations of the antitrust laws, which has been to contract the scope of per se violations and to expand the application of a rule of reason approach when it is unclear whether the type of restraint involved actually restricts competition and decreases output.[4] The proposed legislation, in contrast, eliminates the possibility of analysis of sources of effective competition in individual cases, which seems a highly dubious course.

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[3] United States v. Terminal R.R. Ass'n, 224 U.S. 383 (1912); Associated Press v. United States, 326 U.S. 1 (1945); Otter Tail Power Co. v. United States, 410 U.S. 366 (1973); and MCI Communications Corp. v. AT&T, 708 F.2d 1081 (7th Cir. 1983), cert. denied, ___ U.S. ___, 104 S. Ct. 234 (1983).

The legislation also would be inefficient from an administrative standpoint. It would require the courts to become involved in the difficult and time-consuming process of setting railroad rates on a regular basis, a task the courts are not well equipped to handle. This also raises the possibility that a single railroad may have to face conflicting standards set by different courts for different shippers on its lines.

The legislation might also injure railroad efficiency to a significant degree. Commentators generally agree that past inflexible rail rate regulation weakened many firms and led to serious deterioration of the rail infrastructure.[5] Regulation of the sort required by this legislation could have similar effects. For example, the legislation would require rail carriers to offer their facilities to competitors on terms deemed reasonable by courts of law not necessarily expert in rail accounting principles. In the long run, if railroads are forced to share facilities on terms that do not fully reflect their opportunity cost, this will reduce incentives for new capital investments to improve existing facilities or to construct new facilities. An excellent example of what happens when property owners are unable to retain all the benefits of investments in capital assets can be found within the rail industry itself. The requirement that freight cars be mandatorily interchanged among railroads at non-market-determined rates caused the railroads to purchase low quality freight cars and hindered technological advances in freight car design.[6]

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[4] NCAA v. Bd. of Regents of Okl., 104 S.Ct. 2948 (1984); Broadcast Music, Inc. v. Columbia Broadcasting Systems, Inc., 441 U.S. 1 (1979); Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977).

[5] See, e.g., Theodore E. Keeler, Railroads, Freight and Public Policy (Washington: Brookings Institution, 1983).

[6] According to one study, "an investment in the improvement in quality will not pay off to the owner of the car because the additional returns that are generated by the improvement are collected by other roads." Yehuda Grunfeld, "The Effect of the Per Diem Rate on the Efficiency and Size of the American Railroad Freight Car Fleet," Journal of Business, January 1959, p. 73.

In addition, the legislation would require courts to set rates on covered track and other rail facilities according to an arbitrary formula that might actually increase the cost of rail transportation to shippers of bulk commodities. The prescription for rate-setting, although far from clear, apparently would require rail rates on bulk commodities to make a contribution to overhead in direct proportion to their volume relative to the volume of other traffic on the line. There are at least two reasons to question the wisdom of this prescription. First of all, different commodities can impose different costs on rail assets that are completely unrelated to shipping volumes. Movements of very dense commodities such as coal might increase track maintenance costs, for example. Other commodities might require special loading facilities. Differences in requirements for capital investments by railroad should be reflected in differences in rates, whether or not they correspond to volume levels. Secondly, some attention to differences in demand may very well be in the long run interests of shippers of bulk commodities. If the short term effect of this prescription were to lower the rates on bulk commodities, railroads might have to raise rates on other commodities, and it is not at all clear that other commodities would continue to move by rail at higher rates. A reduction in the volume of other commodities would force shippers of bulk commodities to bear an even greater share of the burden of common costs, leaving them potentially worse off than they were initially.[7]

Moreover, the inflexibility of judicially-determined rates in the face of changing conditions of supply and demand might further reduce the chances for efficient rail operations. During periods of high economic activity such rates might lead to transportation shortages if their inflexibility caused them to be too low. During economic downturns they might reduce demand for rail transportation still further because they would then be too high.

By direction of the Commission.

James C. Miller III
Chairman

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[7] Because violations of the legislation's proscriptions may actually enhance consumer welfare, treble damages are not appropriate here. The danger with this legislation is that treble damages may deter behavior that is on balance pro-competitive.

TESTIMONY ON S.447
of
RONALD G. WASSON
VICE PRESIDENT - PURCHASING
KANSAS CITY POWER & LIGHT COMPANY

Before the
SENATE COMMITTEE ON THE JUDICIARY

MR. CHAIRMAN: I am pleased to be able to present written testimony to this Committee on a problem concerning those dependent upon railroads for transportion and who are victims of monopoly practices in today's deregulated rail transportation marketplace.

Kansas City Power & Light Company (KCPL) is a medium size electric utility and the corporate successor to one of the world's first electric companies, generating electricity since 1882. Headquartered in downtown Kansas City, Missouri, the Company generates and distributes electricity to about 363,000 customers in a 4,700 square mile area located in all or portions of 23 counties in western Missouri and eastern Kansas. Population of the service area is about 825,000.

KCPL operates four coal fired power plants providing most of the Company's electric generation. During 1984, 6.6 million tons of coal were shipped by railroad to these four plants at an estimated cost of $80 million.

The purpose of my testimony is threefold:

1. To express support for S.447, the Railroad Antimonopoly Act of 1985.
2. To discuss KCPL's experience as a captive shipper since passage of the Staggers Rail Act.
3. To demonstrate the ICC's failure to implement the provisions of the Staggers Rail Act intended to provide protection for captive shippers.

I strongly support the concept embodied in this bill.

Full application of the antitrust laws to the railroad industry is appropriate in today's transportation marketplace. This bill would provide those captive shippers who are subject to railroad monopoly power an avenue of obtaining relief from excessive rail freight rates. The burden of excessive rail rates is borne by the customers of KCPL as a portion of their monthly electric bill.

Shipper captivity is not an illusory concept as other witnesses in these proceedings have alluded, but it is a real and significant problem. All four of our coal fired generating plants are dependent on a single railroad for delivery of coal supply.

KCPL presently ships 5.3 million tons of Powder River-Wyoming coal annually to its electric generating stations in the Kansas City area. Each shipment generally consists of 110 KCPL-owned coal cars, each loaded with about 100 tons. These 11,000-ton movements traverse the 1600-mile round trip route each 4.8 days. Barge transportation is not available from arid Wyoming. Truck transportation is available but it would take some 774 trucks carrying 25 tons each, traveling at 55 miles per hour, 24 hours per day, 365 days per year, to deliver the annual 5.3 million tons required. That would space the trucks about 12,000 feet apart in a continuous two-way stream up and down the highway between Wyoming and Kansas City and a truck would meet another going the other way every 1.2 minutes. Air transportation quite obviously is not a practical means of shipping large quantities of coal to remote power plants. Consequently, KCPL is captive to the railroads for coal shipments and more importantly captive to specific railroads when only one railroad has access to the mines and plants involved.

KCPL's electric customers have been adversely impacted by the Interstate Commerce Commission's refusal to enforce provisions of the Staggers Rail Act pertaining to captive shippers. KCPL's experience under ICC Administration of the Staggers Act can be typified by the events at Iatan Station.

In May of 1980, KCPL entered into a pre-Staggers Act agreement for delivery of coal to Iatan from the Powder River Basin. Burlington Northern filed tariffs in late 1981 posting a 15 percent rate increase above contract rates which had been adjusted for inflation. KCPL brought suit against Burlington Northern in Federal District Court to enforce provisions of the May, 1980 agreement. The court found that KCPL did have a contract, however, it was unenforceable because the parties had failed to clearly state the term of duration.

KCPL then filed a complaint case with the ICC in an effort to protect our customers from this unwarranted increase. The Commission determined that the Iatan rate passed the market dominance test, all parties having agreed that KCPL was paying a revenue to variable cost ratio above the Staggers Act threshold test for ICC jurisdiction. The ICC determined the rate to be "reasonable", apparently ignoring Staggers Act guidelines, and would not order an investigation asserting the Burlington Northern was revenue inadequate. KCPL met the criteria established in the Staggers Act but was denied the protections afforded captive shippers as a result of ICC administrative action. Consequently, the freight rates at Iatan have risen 47 percent since passage of the Staggers Act. The ICC's record of finding such rates reasonable was summarized by one of its own law judges who said in May, 1983 that the Commission has no intention of finding a rail rate "no matter how high, to be above a maximum reasonable level."

The recent availability of competitive rail service to some mines in the Powder River Basin has provided KCPL the opportunity to use competition to break the stranglehold of Iatan rail captivity but significant barriers are faced because only a single railroad can make deliveries. In an effort to free Iatan from captive shipper status, KCPL is investigating construction of a rail bridge across the Missouri River to gain access to a competitive rail carrier.

The impacts of shipper captivity at Iatan are illustrated by our economic studies which show construction of a $28 million rail bridge would produce significant savings for our customers through lower freight rates (considering the costs of construction and ownership) by providing competition for the freight. Theoretically, under Staggers Act provisions, the construction of a bridge would not be required since the Act provides for ICC regulation where competition is not available. However, under current ICC regulatory policy of ignoring the needs of captive shippers, the only practical alternative available is the expensive construction of a bridge to open up competition.

Another example of the impact of being a captive shipper can be seen by comparing the results of recent rate quotations at captive and non-captive plants. KCPL also recently requested freight rate quotations for our Hawthorn plant, a non-captive plant about 60 miles farther than Iatan from Powder River Basin coal sources. The rates quoted to Hawthorn were some 20 percent lower than the captive rate quoted at Iatan even though the plant is farther from the coal source and requires significantly longer times to perform coal train unloading.

The ICC implementation of the Staggers Rail Act has subverted the protections provided in the Act for captive shippers. As illustrated by the results in our own Iatan protest case, the Commission blindly focuses on a single issue, revenue adequacy, to the exclusion of all other factors.

Those who state that the Staggers Act is working properly are fond of quoting that the Commission has ruled in favor of the shipper in 50 of 68 captive commodity cases. In fact, the Commission found market dominance in 50 of 68 cases denoting that captive shippers were in fact subject to monopoly power - but the record of final decisions by the Commission is far less favorable. Since passage of the Staggers Act, no coal shipper has prevailed in a final decision by the Commission.

The ICC has promulgated draft coal rate guidelines in the Ex Parte 347 proceedings which allow rates to be increased by an amount 15 percent above inflation until they reach "stand alone cost" or the point where the shipper could build, own and operate his own railroad more economically.

In a recent ICC decision in Docket No. 39687 dated April 15, 1985, involving Platte River Power Authority, the administrative law judge determined the rate paid by Platte River Power Authority to be in excess of "stand alone cost" as proposed by the ICC's Ex Parte 347 Coal Rate Guidelines. Stand alone costs include all relevant costs of owning and operating a private railroad, consequently the variable cost is already included in that figure. Inexplicably, the administrative law judge added the variable cost of the carrier involved to the "stand alone cost" developing an artificial rate limit higher than the rate being paid by the captive shipper. This "double count" typifies the incompetent performance of the ICC which myopically focuses on the single issue of revenue adequacy without regard to the broader public interest of electric consumers who pay monthly for this uneven treatment.

S.447 is an effective means of addressing the abuse of monopoly power by the railroads and providing captive shippers some measure of the protections intended by the Staggers Rail Act. Passage of S.447 will not directly impact KCPL's profitability but it would directly and significantly reduce the electricity bills of our customers and those of countless other utilities who are captive shippers.

THE RAILROAD ANTIMONOPOLY ACT OF 1985

S. 447

THURSDAY, AUGUST 29, 1985

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Waterloo, IA.

The committee hearing was held on August 29, 1985, commencing at 1:40 p.m., at the Waterloo City Hall, 715 Mulberry Street, Waterloo, IA. Hon. Charles E. Grassley (acting chairman) presiding.

OPENING STATEMENT OF SENATOR CHARLES E. GRASSLEY

Senator GRASSLEY. I'd like to get started. This issue is so important that I want to take what time is necessary to get as much information as I can on this issue.

I want to thank everyone for being here today as we discuss S. 447, a bill introduced by Senator DeConcini, which was referred to the Committee on the Judiciary.

According to the supporters, the goal of this bill is to foster competition in the rail industry and bring fair treatment to captive shippers and, ultimately, to the public by bringing the rail industry clearly within the scope of antitrust laws.

Now, I think everybody who's a part of this bill has been very clear in what they're attempting to do, and I think the bill is clearly enough written that nobody makes bones about what it would accomplish. And from that standpoint, maybe because everybody has been so open, some controversy has developed. But there has also been a willingness on everybody's part to discuss some very basic issues that maybe wouldn't otherwise have been discussed if there had been some bill with subterfuge written into it.

The heart of the bill provides that it shall be unlawful for an owner rail carrier to monopolize or attempt to monopolize, by denying or threatening to deny, to any shipper, or another rail carrier, the use, on reasonable terms, of a railroad facility. This facility must be the sole facility over which such shipper can move bulk commodities by rail to connect with the track of a competing rail carrier or to reach the destination of shipment.

Over the past few months, I have heard from several persons representing different groups regarding the issue of the captive shipper rail service, which S. 447 is designed to address.

I decided to hold this hearing to review those concerns and how the passage of this legislation might affect the State of Iowa. It is my hope that by our witnesses' participation today, we will better understand the problems facing the shippers and the railroads, now that the Staggers Rail Act is being implemented, and as a result of that, to determine if there is, in fact, a need for legislation at this time.

Probably for those of you who have been asking me to cosponsor this legislation, it's been a frustratingly long time, but a hearing like this is beneficial, whether or not I cosponsor the legislation. I have no preconceived notions regarding this issue and hope that your testimony will shed some light onto the subject.

Before I call our first witness, I would like to make some general administrative comments. I assume that the record will be open for 14 days. Now, the purpose of leaving the record open for 14 days is so that people who have not been invited and have an interest in this subject would have an opportunity to submit written testimony.

Also, members who can't be at today's hearing may have questions in writing that they will submit to you. If that be the case, we would appreciate it if you return your responses within that 14-day period of time, as well.

One other thing. We have asked that you summarize your statement to 5 to 7 minutes. Now, that does not keep the entirety of your statement from being printed in the record.

I would like to welcome our first witness, Andy Varley. Andy is chairman of the Iowa Commerce Commission in Des Moines, and I want to thank him for being here this afternoon. And of course, he is in the middle of a lot of these issues that affect the legislation before us. And for those of you who don't know Andy as I do, Andy was speaker of the house of representatives my last term in the Iowa House of Representatives, 1973 to 1974. He was a very good legislator, obviously shown by the fact that his colleagues made him speaker of the house at that point.

So with those introductions, I'll just tell them you're a good farmer and good family man. But let's let it go at that.

STATEMENT OF ANDREW VARLEY, CHAIRMAN, IOWA STATE COMMERCE COMMISSION

Mr. VARLEY. Thank you, Senator. I do appreciate the opportunity to be here and express our views and concerns about Senate bill 447. We have a significant interest in this bill and in the Staggers Rail Act and the Interstate Commerce Commission's interpretation of the Staggers Rail Act. We're concerned with present pricing policies, but even more alarmed at potential increases in the future.

Our interest is twofold. First, our major responsibility is regulation of the utility rates. The largest component of those rates in Iowa are electric bills. A major component of the electric bills is the freight charge for hauling fuel to generating plants.

Iowa utilities are heavily dependent on western coal, primarily from Wyoming. The cost of freight now exceeds the cost of the coal at the mine mouth. The volume of traffic from the western coal fields to the midwestern utilities has grown dramatically the past several years. The type of service required is ideal for rail transportation. The coal is hauled on unit trains, the tonnage is high, and the trains run the year round. Don't be misled by data showing that rates of coal transportation have gone up more slowly than other rates. As the volume of coal traffic has increased, there's good reason to expect those rates to go down. Not only has the number of coal trains increased, but keep in mind that the utilities, in most cases, actually own the trains.

The Iowa Commerce Commission also regulates grain dealers and grain warehouses in Iowa. In these troubled times, it requires every effort to keep those elevators financially healthy and to derive the maximum price for their farmer customers. Grain shipments out of the State aren't nearly as high as we would like to see. We anticipate that at some point our foreign markets will revive and there will be need for expanded shipments out of the Midwest. While grain elevators may not be considered captive shippers, since they can use trucks, the charge for trucking becomes the standard. We are concerned that when this happens, the railroads will be in a position, under present ICC policy, to raise the rail rates to just under the cost of trucking grain, extracting excessive revenues that should be going back to the grain elevators and the farmers.

As the Commerce Commission understands this bill, S. 447, it would amend the Sherman Act to grant certain bulk shippers the right to use individual actions in Federal court to apply Clayton Act penalties to monopolizing by rail carriers. Although we have not had time for an indepth review, we question whether it is appropriate to make captive shippers, like many of the Iowa utilities, use individual actions in Federal court to enforce what is, essentially, a ratemaking problem. There are many important technical phrases used in the act, including "generally accepted principles regarding just and reasonable rental of track, bona fide competition, and fair return on prudent investment." Rather than allowing numerous Federal district courts to interpret those ruling terms, it would be better to simply amend the Staggers Rail Act to force the ratemaking body, the Interstate Commerce Commission, to set the correct rates in the first place.

The basic problem is that the Interstate Commerce Commission's interpretation of the Staggers Rail Act encourages the railroad carriers to exercise monopoly power wherever they have it. As an example, consider the situation faced by Wisconsin Power & Light Co. This utility has three coal-fired plants which are captives of their railroad shippers. It also has three plants which can choose between barge and railroad shipping. The captive plants have seen their rates rise substantially faster than the benefits to the plants that benefit from competition.

Between 1979 and 1984, the average per-ton freight rate for the captive utilities rose almost 85 percent, while the freight rates of the other three plants rose only about 15 percent. As a result, the overall cost of the coal burned at the captive plants rose twice as fast over the same time period as at the other plants. We want to make it clear at this point that the issue is not how fast rates in general are rising, but how much faster they rise where there is no competition. This raises the fear of predatory pricing. The railroads are tempted to overcharge their captive customers in order to support below-cost rates along competitive lines. The result is unfair competition for barge traffic, for example, and a higher overall cost of transportation.

In other words, the problem is not that rail shipping rates in general are too high. The problem is that rates are too high wherever there is no competition. Railroads are exercising monopoly power, and the end result is that customers of electricity pay higher rates than they should. Utilities that have no real coal transportation alternative to railroad transportation are captive shippers. They are completely vulnerable to independent railroad pricing action uncontrolled by effective intervention by the Interstate Commerce Commission.

The fundamental problem is that the Interstate Commerce Commission does not regulate railroads based on the cost of providing the service. Instead, it uses a revenue-adequacy concept which was rejected for use for utilities over 100 years ago. We feel that the Staggers Rail Act was intended to encourage competition where it is viable, but to use cost-based ratemaking for the protection of captive shippers. Competition can set the rates only where it exists; however, the Interstate Commerce Commission should be required to set rates based on costs where competition is absent.

The heart of the Interstate Commerce Commission guidelines is the stand-alone cost test, which states, in effect, that rates are not unreasonable unless they exceed the cost to the shipper of building its own railroad. They also use the new replacement cost of the entire system as a standard for rate base used in calculating the appropriate earnings. They use the current interest rates to calculate interest costs, rather than the actual interest paid. The result is the overcharging of captive customers. They pay more than the costs incurred to serve them (costs which include a reasonable profit for the railroad). When there is an alternative form of transportation, the price is based on the alternative and may be unrelated to cost.

We are in full support of financially strong railroads. We simply do not want to be in the position of being overcharged to subsidize other railroad customers or overcompensate the railroads. Thank you, Senator.

[The prepared statement follows:]

SUPPLEMENTARY COMMENTS FOR FIELD HEARING ON THE SUBCOMMITTEE ON ADMINISTRATIVE PRACTICE AND PROCEDURE HELD AUGUST 29, 1985, CITY HALL, WATERLOO, IA

The Iowa State Commerce Commission (Iowa) appreciates this opportunity to supplement its comments made at the field hearing conducted on August 29, 1985, at the City Hall in Waterloo, Iowa. As stated in Iowa's original comments, Iowa has a significant interest in the Staggers Rail Act and in the Interstate Commerce Commission's interpretation of the Staggers Rail Act. Iowa believes that the hearing documented numerous examples of overcharging of captive shippers under the present law. Iowa believes the potential for this is even greater if Congress fails to redirect the Interstate Commerce Commission.

At the hearing, Senator Grassley requested that Iowa submit certain additional comments, including an analysis of Senate Bill 477, sometimes known as the "Coalition Bill." Iowa generally favors the basic goal of this bill, which is to require that the Interstate Commerce Commission regulate in an effective manner whenever that is necessary, and leave the rest of the industry to the marketplace. This, Iowa believes, conforms with the original intent of the Staggers Rail Act.

Specifically, Iowa favors three proposals contained in S. 477. First, the bill would establish a more reasonable method for determining "market dominance." If a shipper is served by only one rail facility, market dominance would be presumed, and the burden of proving otherwise would shift to the rail utility. Second, the bill would redefine "revenue adequacy" in a manner which would result in much more reasonable revenue requirements for the railroads. Revenue adequacy would be determined using straight-line depreciation of original costs, excluding deferred tax reserves, and the cost of capital would be determined from the actual cost of embedded debt along with reasonable estimates of the cost of new equity. This method, which is essentially the same as the method used in setting other utility rates, would result in a realistic determination of revenue adequacy. Finally, S. 477 would create better procedures for determining "rate reasonableness." The burden of proof would be on the railroad, and the Interstate Commerce Commission would be required to make certain affirmative findings when approving rates. If a certain rate is to be set higher than the fully-allocated cost of providing the service, the ICC would be required to find that (a) the higher rate is needed to maintain or achieve revenue adequacy and (b) the rate is still no higher than it would be if all captive traffic were forced to pay a subsidy to ensure revenue adequacy. In other words, no single captive shipper could be charged more than its fair share of the cost of keeping the railroad financially sound. This is very important; it would deter predatory pricing by the railroads, by making it more difficult to charge excessive rates to captive shippers.

At the same time, the ISCC does not support every provision of S. 477. It appears that the proposal has become too broad. Iowa would prefer a clean, simple approach directing the Interstate Commerce Commission to do what the Staggers Rail Act intended: deregulate the industry where a competitive market exists, while effectively regulating to protect those shippers not protected by competition.

Senator Grassley also asked whether the example cited in Iowa's comments, relating to the Wisconsin Power and Light Company, is an isolated instance. There is probably no other example which so clearly demonstrates the problem. It is relatively rare for a utility to have some plants located where they may take advantage of competitive transportation and also have plants where they are captive shippers. However, there is no reason to believe that the magnitude of the problem demonstrated is any different for this example than for other utilities which are captive shippers. There may not be any other examples which demonstrate the problem as well, but Iowa believes that the actual problem demonstrated is wide spread. Captive plants are simply being overcharged.

Respectfully submitted,

ANDREW VARLEY,
Chairman, Iowa State Commerce Commission.

Senator GRASSLEY. Thank you very much, Andy. In regard to your consideration of the impact upon utility rates, where does most of the coal used in Iowa for utilities come from?

Mr. VARLEY. Most of the coal is western coal, and most of that comes out of Wyoming.

Senator GRASSLEY. When you say "most," about how much, roughly?

Mr. VARLEY. Eighty-five percent; in that range. The utilities would probably have specific numbers on that.

Senator GRASSLEY. And then the railroads that would deliver that coal would be?

Mr. VARLEY. Primarily the Burlington Northern. The Union Pacific may be picking up on some of that. And for part of the shipment, North Western.

Senator GRASSLEY. Would the Burlington Northern deliver practically all the coal, then, that comes from——

Mr. VARLEY. Yes, essentially.

Senator GRASSLEY [continuing]. From the West?

Mr. VARLEY. Yes.

Senator GRASSLEY. What percent of the electrical power is supplied by coal in Iowa?

Mr. VARLEY. That depends on how much power the nuclear plants are running at any given time. I think the latest firm figure we have is about 85 percent was coal in 1982. Since that time, we've had the Louisa plant going, which is coal fired. And really, depending on the status of nuclear plants, we would be in that range.

Senator **Grassley**. What's the range, again?

Mr. **Varley**. About 85 percent.

Senator **Grassley**. Of coal?

Mr. **Varley**. Yes.

Senator **Grassley**. Would you estimate the total overcharges to electrical consumers, resulting from our utility status as a captive shipper?

Mr. **Varley**. I can't give you any real good figures on that. At the present time, we think there is a substantial overcharge of several million dollars. As I said in my comments, we're much more concerned about the potential in the future if the coal-shipping rates continue to go up. And the utilities really have no choice, if they're faced with those higher rates, except to pay those higher rates.

Senator **Grassley**. So, at this point, it has not become a serious problem, but it could become a serious problem?

Mr. **Varley**. The cost today appears to be many millions of dollars, and I think the specific utilities could give you what they would view as appropriate numbers. It's a serious problem today. The potential prospects in the future are much worse.

Senator **Grassley**. Then I stand corrected. Even in your judgment, it's a serious problem today, but destined to become much more serious?

Mr. **Varley**. That's right. And one reason that it's not such an obvious problem is that it's a pass-through cost. Electrical customers are required to pick up that cost, and they are not aware of the source of part of the cost of those electric rates.

Senator **Grassley**. Do you feel that the Interstate Commerce Commission has the power to use the cost of providing the service concept that you mention in your remarks and not the revenue adequacy concept that you indicated they presently use? And has Congress given the ICC too much leeway to interpret the Staggers Act? But, before you answer that, let's just say, if so, should we adopt specific legislation requiring the ICC to use other criteria in these rate disputes? And is this approach feasible to the antitrust approach taken in S. 447?

Mr. **Varley**. To begin with, I think the Staggers Rail Act could be very workable with what we would consider appropriate interpretation by the Interstate Commerce Commission. As I said, it is a ratemaking question, where there is monopoly power, where there is a captive shipper, and shipping rates based on cost of service. I think that approach is preferable to going with the antitrust action. There's so much potential for different interpretation in different jurisdictions. Some of these phrases that are used in the legislation are very vague and would be subject to a wide range of interpretation by the judges. There wouldn't be any standard, except that you can put a captive shipper in a position of facing an antitrust action that could take 10 or 12 years. If shipping rates are critical to their existence, they're going to be out of business long before they get any settlement on an antitrust action.

I guess the question is, Is anything likely to happen if it's left up to the ICC to change their policy? I doubt if it is, short of legislation. Unless there's some dramatic changes in the ICC, I think legislation by Congress would be necessary to change that policy.

Senator GRASSLEY. With regard to the latter, then, you would suggest some approach other than making the antitrust laws applicable, because you're saying that that would really be too long of a decisionmaking process in the courts in order to protect the consumer?

Mr. VARLEY. That's right.

Senator GRASSLEY. You prefer administrative action, but you don't think administrative action will happen?

Mr. VARLEY. We have not observed any change by the ICC that would indicate they're going to make domestic changes.

Senator GRASSLEY. So some leadership by Congress, but not in this direction?

Mr. VARLEY. That would be our preference.

Senator GRASSLEY. Have you seen any other congressional action that you like?

Mr. VARLEY. We have seen a number of other proposed bills, and I'm not fully aware of those right now, in terms of details and specific legislation. But the bills I've seen—the coalition bills—really include far more issues than I think they should. I think some simple legislation by Congress would make a lot more sense for solving the problem.

Senator GRASSLEY. S. 447, the bill we deal with here, is an antitrust approach and kind of a Judiciary Committee approach. Another approach is S. 477. That's a Commerce Committee approach. You couldn't speak to that one at this point?

Mr. VARLEY. I can't speak to the details.

Senator GRASSLEY. I might ask you to submit a statement on S. 447 based upon your feeling that congressional action is probably going to be necessary and your view that antitrust legislation takes too long and your view that the ICC won't act, even considering that's preferable. Or if there are other approaches that I'm unaware of, that are embodied in proposed legislation, I'd ask you to make a brief comment on those as well.

Mr. VARLEY. Very good.

Senator GRASSLEY. Do you have any further comments you want to make? I'm done with my questioning.

Mr. VARLEY. No; I think we're agreeable.

Senator GRASSLEY. Thank you very much.

Our next group is a panel. I'd like to have Tom Pitner, general counsel and vice president of the Iowa Electric Light & Power in Cedar Rapids, testify first. Then he'll be followed by Dean Stoll, manager of the fuel supply of the Iowa Public Service in Sioux City; and then Ken Purcell, who is the government affairs coordinator for the Iowa-Illinois Gas & Electric in Davenport; and then Jerry Parkin, who's manager of government affairs at the Iowa Power & Light Co. It may be a little crowded up here, but let's see how it works out. Usually we go through all your statements, then I ask questions of the entire panel. So if we can get two people at the table, and then if the people on the extreme right and left can just squeeze into the triangle there, I think we'll be all right. You might have to use the other table here.

Would you like to start, Mr. Pitner?

Mr. **Pitner**. I sure will, Senator. Thank you. The proximity of my fellow panel members allows us to communicate with elbow language.

Senator **Grassley**. Well, I can see that.

STATEMENT OF PANEL CONSISTING OF: THOMAS J. PITNER, GENERAL COUNSEL AND VICE PRESIDENT, IOWA ELECTRIC LIGHT & POWER, CEDAR RAPIDS; DEAN F. STOLL, FUEL SUPPLY MANAGER, IOWA PUBLIC SERVICE, SIOUX CITY; KEN PURCELL, GOVERNMENT AFFAIRS COORDINATOR, IOWA-ILLINOIS GAS & ELECTRIC, DAVENPORT; AND JERRY D. PARKIN, MANAGER OF GOVERNMENT AFFAIRS, IOWA POWER & LIGHT CO.

Mr. **Pitner**. Thank you, Senator, for allowing us the opportunity to give you our comments on a very timely and appropriate bill.

Iowa Electric Light & Power Co. provides electricity to more than 204,000 residential, commercial, industrial and rural customers in 55 counties, including 272 incorporated cities and 120 unincorporated communities. The company also delivers steam for heating and industrial purposes in Cedar Rapids, which is fired by coal, Cedar Rapids being the location of the company's headquarters.

The company operates three coal-fired plants: Sutherland Station in Marshalltown, IA, and Sixth Street station and Prairie Creek station in Cedar Rapids, IA. The company owns an undivided 15 percent of the Ottumwa generating station coal-fired unit operated by Iowa Southern Utilities Co., and has a 10-year power purchase contract with the city of Muscatine in unit No. 9 of the Muscatine generating plant, also a coal-fired unit.

Of the total electricity sold by the company in 1984, 35 percent was purchased from other utilities, using a combination of fossil, hydro and nuclear fuels, while the balance of 65 percent was provided by the company's generating stations, of which coal-fired units provided a little over 22 percent. We do have a nuclear power based station, also. But for the years 1985 through 1987, it is expected that coal will be the fuel used to provide, on the average, 30 percent of the company's electricity sales.

Iowa Electric estimates that existing coal-fired generating units providing electricity for the company's customers will require in excess of 3½ million tons of coal during the 1985 to 1987 period.

The majority of the company's coal is delivered by rail. I should say the significant portion of the company's coal is delivered by rail. Iowa Electric and its customers, as well as the customers of the generating stations of which Iowa Electric is a joint owner, have an intense interest in the access to competitive transportation opportunities. Present regulation by the ICC, under the Staggers Rail Act of 1980, has not afforded Iowa Electric or its customers access to competitive transportation, due to a prorailroad attitude in the interpretation of the Staggers Rail Act. Even where alternate carriers are available, rates do not reflect competition due to the focus on coal as a subsidy to other operations.

In light of railroad abandonments and mergers in the Iowa and midcontinent area not served by major waterways, the monopoly position held by the railroads in many areas and the lack of shipper-protection regulation, Iowa Electric is supportive of modifications to the Staggers Rail Act. Specifically, the burden of proving lack of market dominance should be shifted to the railroad industry, and the burden of proving railroad inadequacy should be stiffened by closer adherence to standard ratemaking and accounting procedures, as well as generally accepted economic principles of regulated monopolistic pricing.

While S. 447 acknowledges that severe difficulties exist in bulk rail shipments, it amends the Sherman Act, rather than the problematic Staggers Rail Act. Clearly, fairly established railroad rates is the goal of both S. 447 and S. 477. However, amending the Sherman Act to address the problems created by the Interstate Commerce Commissions interpretation and enforcement of the Staggers Act is not Iowa Electric's preferred legislative approach.

H.R. 1190 and S. 477 are supported by Iowa Electric, in that they presume market dominance in all cases where a shipper is served by a single carrier, unless that carrier can show that effective competition from other carriers or modes of transportation exists. Alternative product and geographic competition, which are irrelevant factors, in our opinion, would no longer be used in determining market dominance. Under the proposed new rate-reasonableness standards, railroads with captive shippers would be subject to an economically realistic allocation of costs that would be more protective of captive shippers and would replace the current "stand alone" test—that Mr. Varley testified to—that employs an avoided cost or marginal cost philosophy that is not reflective of marketplace realities.

Iowa Electric's position concerning the Interstate Commerce Commission's current regulations of railroad rates and prices is well stated in our testimony before the ICC on different rate applications by the railroads, and I have attached a document that does present those positions. Very often, the petitioning railroad requests an outrageous increase, knowing that the ICC will grant a major proportion of that increase. The shipper—in our case, the utility—who needs that coal in order to stay within its obligations to serve and obligations of contracts to take coal, will fight it, knowing that they will not be very successful, hoping for even a 10- to 20-percent reduction, often accepts 10 percent in order to get on with its business, knowing that the prorailroad stance of the Interstate Commerce Commission will prevail. In this process, the utility customer has very little representation. Quite honestly, the utilities are bound by contracts to take, and they have tc get their coal from the mine to their plants. The resulting settled rates are still 20 to 40 percent too high because of the lack of meaningful alternate choices. Iowa Electric's customers pay that excess and have no representation in the process, save for the utility's efforts.

[Interstate Commerce Commission brief follows:]

On behalf of Iowa Electric's customers, we sincerely offer this statement and any other information required of us in order to remedy the present inequities and diseconomies delivered by the Interstate Commerce Commission. Thank you very much.

Senator GRASSLEY. Thank you.

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Iowa Electric Light & Power Company, :
:
Complainant :
:
v. : I.C.C. Docket No. 38223
:
Burlington Northern Inc., et al., :
:
Defendants :

REPLY OF IOWA ELECTRIC LIGHT & POWER COMPANY TO THE RAILROADS' MOTION TO DISMISS

Iowa Electric Light and Power
Company

By: John M. Cleary
Nicholas J. DiMichael
DONELAN, CLEARY, WOOD
& MASER, P.C.
914 Washington Building
Washington, D.C. 20005
(202) 783-1215

Attorneys

Of Counsel:

DONELAN, CLEARY,
WOOD & MASER, P.C.
Washington Building
Washington, D.C. 200005

Dated: August 13, 1981

Due Date: August 13, 1981

Comes now Iowa Electric Light & Power Company (Iowa Electric) and replies to the "Motion to Dismiss" filed by the defendants Denver & Rio Grande Western Railroad Company (D&RGW), Illinois Central Gulf Railroad Company (ICG) and Union Pacific Railroad Company (UP) dated July 24, 1981. In Reply, Iowa Electric respectfully states as follows:

Procedural Background

On March 27, 1981, Iowa Electric filed its "Verified Complaint" in this proceeding pursuant to Section 229 of the Staggers Rail Act of 1980. The Complaint challenged the rates for the transportation of coal to Iowa Electric's coal-fired generating units at its Sixth Street Station and its Prairie Creek Station located at the railroad destination of Cedar Rapids or Crandic, Iowa. The challenged coal rates initially covered by the Complaint involve coal originated in Colorado at either Craig or Empire and coal originated in Illinois at either Dunfermline or Spartan Mine, Illinois. With respect to the latter movements from Dunfermline and Spartan Mine, Illinois, on July 23, 1981 an "Uncontested Motion To Dismiss" was filed by the complainant and certain mid-western railroad defendants (Chicago, Milwaukee, St. Paul and Pacific Railroad Company, Missouri Pacific Railroad Company, and Burlington Northern Railroad Company) stating that these companies had stipulated that the Commission may dismiss the named mid-western railroads from this complaint proceeding. This removes from the case any issue as to the lawfulness of the rates from Dunfermline and Spartan Mine.

On June 24, 1981 the Commission served a "Notice to Defendants" dated June 3, 1981 in this proceeding which called upon the defendants to satisfy or answer the Complaint within 30 days from that service date and called for the defendants to respond to four questions, the same questions that have been put to the defendants and the complainants in the various Section 229 Complaints.

Those defendants, which remain in the proceeding after the uncontested Motion to Dismiss certain mid-western railroad defendants, have not filed an answer, verified or otherwise. Rather, under date of July 24, 1981 the D&RGW, the ICG, and the UP (the railroads participating in the movement of coal from Craig and to Empire, Colorado and the destinations at or near Cedar Rapids, Iowa) filed their "Motion to Dismiss" without any accompanying Verification or accompanying Verified Statement.[1/] The sole basis put forward in the Motion to Dismiss is the assertion, unverified and unsupported, that the defendants lack market dominance over the traffic involved.

[1/] The nature of the Motion to Dismiss makes it appear to be comparable to a Motion for Judgment on the pleadings under Rule 12(c) FRCP.

The Motion to Dismiss was assertedly filed pursuant to Rule 34 of the Interstate Commerce Commission's Rules of Practice, 49 CFR §1100.34.

The Railroads Motion To Dismiss Is Not In Accord With Rule 34

Although the railroads assert that their Motion to Dismiss is filed pursuant to Rule 34 of the Interstate Commerce Commission's Rules of Practice, 49 CFR §1100.34, the Motion fails to meet the requirements of Rule 34. Rule 34, entitled "Motion to Dismiss or to Make more Definite and Certain", provides, in pertinent part:

> "(a) As to Complaint. Defendant may file with his answer, or with his statement under modified procedure, a motion that the allegations in the complaint be made more definite and certain, such motion to point out the defects complained of and details desired. Defendant may also file with his answer a motion to dismiss a complaint because of lack of legal sufficiency appearing on face of such complaint."

Clearly the defendant railroads do not rely upon the first sentence of the quoted portion of paragraph (a) of Rule 34 since there is no request that the complaint be made more definite or certain. Defendants' reliance upon the second sentence of the quoted subparagraph (a) of Rule 34, or any other portion of Rule 34, is misplaced since the defendants clearly have not filed their Motion "with his answer". The filing of an answer is a clearly stated prerequisite to the filing of any Motion to Dismiss under Rule 34.

In addition, the defendants improperly invoke Rule 34 since it is clear from a reading of their Motion that they do not assert any "lack of legal sufficiency appearing on face of such complaint" -- the complaint filed by Iowa Electric on March 27, 1981. Rather, the defendants raise a question of fact, an alleged lack of market dominance, which can not form the basis of a motion to dismiss in the pleadings.

Complainants' Affirmance Regarding Facts Establishing Market Dominance, Which Must Be Accepted As True For The Purpose Of Deciding The Motion, Are Legally Sufficient

Complainants' averments establishing the facts sufficient to support a finding of market dominance (i.e. an absence of effective competition from other carriers or modes of transportation for the transportation to which a rate applies; see 49 U.S.C. §10709(a)) must, for the purpose of deciding the Motion to Dismiss, be taken as true.[1/] A Motion to Dismiss under Rule 34 must be based upon an alleged "lack of legal sufficiency appearing on face of such complaint."

The defendants have filed no answers specifically challenging the averments of Iowa Electric's complaint. In their Motion to Dismiss the railroads did not specifically assert facts that contradict Iowa Electric's affirmance establishing market dominance. The railroad defendants do not assert any facts regarding the ratio of revenue to variable cost as relevant to the threshold jurisdictional levels established in the Staggers Act. In contrast, the complaint avers that the revenue to variable cost ratio on the rate, including surcharge, at the October 1, 1980 level is 172% from Craig, Colorado and 174% from Empire, Colorado. This averment is supported by the verification of Frank S. Harris, a transportation cost consultant and principal in the firm of Snavley, King, Harris and Associates, Inc., Washington, D.C. The complaint contained these unchallenged averments even though it is the burden of the railroads to assert any affirmative defense that a challenged rate does not exceed the threshold

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[1/] Brotherhood of Sleeping Car Porters v. Pullman Co., 139 I.C.C. 741, 742 (1928): "A motion to dismiss admits the truth of all facts well pleaded..."; and Kansas City Southern Ry. v. Kansas City Term. Ry., 211 I.C.C. 291, 294 (1935): "We will proceed upon the ground that the motions to dismiss, for the purpose of determination of the jurisdictional question, admit the truth of all material and relevant facts that are well pleaded, that is, evidentiary facts necessary to the framing of the issues, but not conclusions of fact of or law...".

jurisdictional level called for by the Staggers Act. As indicated, the railroads' Motion to Dismiss does not challenge these averments regarding the ratio of revenue to variable cost.

The railroads' Motion to Dismiss does not challenge the other factual assertions contained in the Verified Complaint which support a finding of market dominance. These unchallenged assertions include:

(1) "The Colorado origin rates at issue were docketed, discussed, considered and approved before the Colorado-Utah-Wyoming Committee of the Western Railroads under 5b Agreement No. 2." (Complaint, paragraph 5)

(2) All of the coal transportation from Craig and Empire, Colorado to Cedar Rapids/Crandic was by rail movement via the defendant carriers..." (Ibid)

(3) "There are no known originating for-hire carriers of any mode offering interchangeable, practicable and economic service between the involved points or areas." (Complaint, paragraph 7)

(4) The defendant railroads have taken all general increases approved by the Commission in the preceeding two years for application on the challenged rates. (Ibid)

These assertions must be accepted as true in deciding the railroads' Motion to Dismiss the complaint based upon the pleadings. It is basic that when a Motion to Dismiss for the lack of legal sufficiency, including lack of jurisdiction is claimed, the assertions of the complaint must be taken as true. See footnote 1 at page 5, supra.

The only factual basis put forward by the railroads as a support for their Motion to Dismiss is a claim, based upon citations and quotations taken totally out of context from another proceeding and significantly misinterpreted, that "Iowa Electric has recently conceded that defendants lack market dominance over the Colorado movements to Cedar Rapids in its April 2, 1980 submission in Iowa Electric Light and Power Company v. Burlington Northern Inc., Docket Nos. 37387 and 37246 (Sub-No. 3(b))." (Motion to Dismiss, page 5) Iowa Electric made no such concession. The quoted statements upon which the railroads mistakenly rely to assert such a "concession" are taken entirely out of context and do not support the conclusion which the railroads would reach.

It is a considerable distortion for the railroads to claim that statements by Iowa Electric's witnesses in other proceedings, including Docket No. 37387 and 37246, can be read as having "conceded that Defendants lack market dominance over the Colorado movements..." (Railroad Motion, p. 5) For convenience we repeat here the statements quoted by the railroads on which they rely for their position. The railroads first quote Mr. Samuel J. Tuthill, Senior Vice President, Energy Resources and Utilization - Research and Environment for Iowa Electric, as having testified in his Statement on April 2, 1980 in Docket Nos. 37387 and 37246 that "Cedar Rapids' [power plant's] projected 1980 coal requirements are 814,000 tons". (Statement at p. 4, Railroad Motion, p. 5) The railroads then subsequently quote Mr. Tuthill's Statements at pages 2-3 that:

> "Colorado coal is not at this time competitive with washed Illinois Basin coals. The SOx standard in Linn Co., Iowa, does not preclude use of mid-continent washed coal and the energy and transportation costs of fuel delivered from the mid-continent is significantly below the delivered costs of Colorado coal. Thus the utility of western coal under IE boilers is lacking. The company is currently negotiating with the Colorado vendor to reduce or eliminate deliveries under the contract. In any event, Western coal is used in limited quantities, and in view of the high cost delivered, the utility of western coal is low for Cedar Rapids power plants.
>
> "With respect to Iowa Electric's power plants in Cedar Rapids, Missouri and Illinois represent the only economically competitive sources of conforming coal." (emphasis added by railroads)

The railroads then combine these quoted statements with the fact asserted in the Complaint that the 1980 rail tonnage to Cedar Rapids and Crandick was 236,545 tons from Craig, Colorado, plus 12,610 tons from Empire, Colorado to support the statement that "less than 250,000 tons of the coal received at the Cedar Rapids power plants has been delivered by defendants from Colorado - i.e., less than 30% of Iowa Electric's estimated 1980 consumption at Cedar Rapids was carried by

D&RGW, UP and ICG." (Railroad Motion, p. 5, emphasis in the original) From these statements the railroads incorrectly argue that "based upon Iowa Electric's expressed concession that D&RGW, UP and ICG lack market dominance over the Colorado movements, the Commission should dismiss at least that portion of the Complaint." (Railroad Motion, p. 6)

First, it is clear that the quoted statements from Iowa Electric's testimony in another case, constitute no "express concession" and do not "concede" that the moving railroad defendants "lack market dominance over the Colorado movements". The fact that a particular destination may receive a product from more than one origin, whether the receipts are by rail or other alternative mode of transportation, does not, in itself, establish that there is an absence of effective competition for the transportation to which a particular challenged rate would apply. Similarly, the fact that a particular destination may receive the same product from more than one origin and have all such movements transported by railroad also does not prove an "absence of effective competition" for the transportation to which a challenged rate applies. The issue is clearly a factual one which centers on the question of what constitutes "effective competition". Specifically, the issue centers on whether or not there is "effective competition" which acts and is effective with respect to 'the transportation to which a rate applies.'" 49 U.S.C. §10709(a), (emphasis added).

The material quoted by the railroads from the Statement of Mr. Tuthill in no way establishes "an absence of effective competition....for the transportation to which (a challenged) rate applies." The railroads themselves assert that:

> "whether effective competition is present so that the marketplace can be relied upon to regulate rates is a question that requires a multi-faceted inquiry into the existence of intramodal, intermodal, source and product competition. The inquiry is essentially a qualitative one, in which the Commission must consider the entire range of options available." (Railroad Motion, pp. 3-4)

Without discussing the propriety of relying upon source and product competition, a reliance which we believe is totally misplaced and incorrect under a proper reading of the statute, it is clear that even the railroads recognize that a "multi-faceted inquiry", presumably into facts, is necessary in order to resolve the question, which is a factual question, as to whether or not there is "effective competition". None of the railroads statements, their arguments, nor the quotations from Mr. Tuthill's statements, establish anything that could be described as "effective competition" which "can be relied upon to regulate rates", i.e., the rates for the transportation to which the challenged rate applies.

The railroads have in no way indicated that the resulting rates from Colorado to Cedar Rapids, Iowa reflect any of the indicia of effective competition. Indeed, the railroads do not even discuss what would be the indicia of effective competition, i.e., the symptoms that "the marketplace can be relied upon to regulate rates". The railroads have presented no rate comparisons with any rates which could be described as themselves reflecting effective competition in the marketplace resulting in truly competitive - effectively competitive - rates. The railroads have presented no cost evidence as to the variable cost or even any total or fully allocated cost which provide no more than market competitive returns on the actual investment to demonstrate that the rates in issue are reflective of "effective competition".

Under the newly-prescribed evidentiary guidelines for determination of market dominance, Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations, 365 I.C.C. 118, served June 24, 1981, the Commission has recognized four major forms of competition which tend to disprove the existence of market dominance. Under the new guidelines the forms of competition are: (1) intramodal competition, (2) intermodal competition, (3) geographic competition, and (4) product competition.[1] Where a a proceeding involves numerous origins and destinations, or a number of either, with service or routing by a variety or a combination of several rail carriers, intramodal competition is not a fact that would be applicable. See Initial Decision of ALJ Richard H. Beddow, Jr., Docket No. 37466, The Aluminum Association, Inc., et al. v. The Akron, Canton, & Youngstown R.R. Co., served August 5, 1981, p. 7.

The railroads' arguments that they lack market dominance is apparently grounded on a contention of geographical competition. "Clearly, geographical competition must be viewed in real world terms and it should not be made the subject of speculative, extreme alternative scenarios". (Initial Decision of ALJ Beddow, Docket 37466, supra, p. 8) Without a showing that the result of alleged geographic competition has been the establishment of rates on the transportation to which the challenged rate applies which are at a level determined by the marketplace reflecting the various indicia of "effective competition", the mere fact that a product, even the coal at issue in this proceeding, can be obtained at a given destination from various origins, including the origin from which the rate is challenged, does not in itself establish the type of geographic competition that would or could be considered as equating with the "effective competition" required by the Staggers Act to rebut an indication of market dominance. It is of no consolation to producers at Point A, who are complaining of the rates between Point A and Point Z, to be told that because the customer at Point Z can also and has, in fact, received some of the same product from Points B, C or D, that, therefore, the rates between A and Z are subject to "geographic competition" so that the I.C.C. lacks any jurisdiction to inquire as to the maximum reasonableness of the rates between A and Z, even though such rates are: (1) far above the cost of service, and do not therefore appear to have been competitively made with other rates on coal from either the same or other origins to the same destination; (2) provide returns far in excess of the average contribution over variable cost which is required to achieve revenue adequacy on the movement for the carriers involved and which "competitors" would be willing to accept; and (3) result in high returns on the actual investment required to provide the transportation, etc.

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[1] Iowa Electric disputes the propriety of the new guidelines, particularly the inclusion under the Commission's decision of what it terms "geographic competition" and "product competition". There is a proceeding before the United States Court of Appeals for the Fifth Circuit where the Ex Parte No. 320 (Sub-No. 2) decision of the Commission is subject to judicial review. Fifth Circuit Nos. 81-4257, Western Coal Traffic League v. United States and I.C.C., and 81-4299, Gulf States Utilities Co., et al. v. United States and I.C.C.

The fact that coal has been received from alternative origins does not establish that there is effective competition for the transportation to assure competitive rates not needing regulation. Nor does the fact of some receipt of coal from alternative origins indicate that the coal moving under the questioned rates could be shifted and received from another origin or that the resulting rate on the challenged movement is reflective of effective competition. Clearly, the railroads ignore the fact that there could be, and in fact are, contractual restraints or other limitations that make it infeasible to transfer or discontinue the Colorado originated coal so as to establish effective competition and resulting reasonable rates on the movement from Colorado.

For example, at present, the contracted Missouri coal cannot be burned at Cedar Rapids in compliance with the SO_2 emission standard of five pounds per MBTU without the addition of the low-sulphur coal required to be obtained from Empire or Craig, Colorado. Absent the coal supply contracts for Colorado coal, Iowa Electric might be able to obtain coal conforming to emission standards and boiler requirements from Mid-Continent sources in Iowa, Missouri and Illinois. However, the fact is that there are existing coal supply contracts requiring shipments from Colorado. Therefore, it is not feasible for Iowa Electric to discontinue the movement from Colorado or to have that volume shifted to other non-Colorado origins.

Long-term contract commitments prevent Iowa Electric from availing itself of any theoretically competitive geographic sources of coal which may exist for the Missouri and Colorado coal burned at Cedar Rapids. Iowa Electric has a ten year contract running from July 1, 1975 to July 1, 1985 for the purchase of a minimum of 250,000 tons per year of coal from the Empire Energy Corporation, Craig, Colorado. Iowa Electric is, therefore, locked in to the transportation of coal from Craig and Empire until at least the middle of 1985. Any alleged "geographic competition" is totally non-feasible and cannot result in the release of Iowa Electric from the market dominance of the railroads moving coal from Colorado.

There is no intramodal competition. While there appear to be two alternate routes for movement from Craig, Colorado to Cedar Rapids, both of them involve the D&RGW the only carrier from Craig, Colorado to Denver. On the segment from Denver to Council Bluffs, Iowa the UP and BN provide competitive routes while the ICG and C&NW provide alternative routes on the segment from Council Bluffs to Cedar Rapids. However, although there are two routes, there appears to be no competition on price - the rate is no lower via the alternate route. As indicated and averred in the complaint, the rates were considered, acted upon and established through rate bureau activity, a fact which also rebuts any concept of "effective competition".

As to intermodal competition, water transportation or slurry pipelines cannot be seriously considered as alternative transportation modes. There is no water route from Colorado to Cedar Rapids. There is no viable talk of any viable slurry pipeline being able to provide this service, certainly not within the term of Iowa Electric's commitment to the movement from Colorado through mid-1985. Alternative truck movement would be totally non-feasible. Based on present deliveries it would take 900 truckloads per month to make deliveries to Cedar Rapids. Based upon a four-day round trip (extremely generous and what could be feasibly accomplished), it would take 120 trucks running seven days a week to transport the volume. Even if such a large volume and such a huge number of trucks could be accomplished in a physical sense, at a minimum, the truck rates would be double the rail rates. Truck competition is clearly not a feasible economic alternative that could be considered as establishing "effective competition".

Nor is there any product competition resulting in "effective competition". The use of natural gas is limited under the Power Plant and Industrial Fuel Use Act. Under 42 U.S.C. §8341(a) Iowa Electric may not use more than its base period 1974-1976 gas usage when there was not more than 20 percent of fuel consumed. Natural gas use is limited to flame stabilization and start-up. The use of natural gas as a primary fuel source is precluded under the Act in the absence of a specific exemption which is not feasible and is not available. The delivered cost for an alternative fuel use of natural gas at $3.04 per MBTU does not provide "effective competition" for the delivered cost of coal from Craig, Colorado, including the rail transportation thereof at the complained of rate, of $2.67 per MBTU. Similarly, the alternative cost of No. 2 fuel oil at $6.86 per MBTU does not provide any effective competition which would hold down or serve to regulate the rates on coal from Craig as complained of in this proceeding.

At its Sixth Street Station, Iowa Electric does burn a "furfural residue", which is an industrial waste consisting of oat hulls. The supply of this product is limited. In the year ending June 30, Iowa Electric burned furfural residue in an amount equivalent to 55,000 tons of coal. This was the total amount of furfural residue that was available.

The Commission is requested to deny the railroads' Motion to Dismiss and find that the railroads possess market dominance, i.e., there is an absence of effective competition for the transportation to which the challenged rates apply.

The Railroads' Recommended Procedure For Deciding The Jurisdictional Questions Raised In This Motion Should Be Rejected

The railroads in their Motion to Dismiss request the Commission follow the concepts set forth in the Notice of Policies for handling the Section 229 Complaints (served April 28, 1981), and treat the jurisdictional issue as a preliminary matter. The railroads further request that they be given certain procedural advantages in dealing with the jurisdiction of question. First, even though the railroads have filed a Motion to Dismiss, they apparently contemplate that there would be the presentation of evidence on the market dominance questions "and other grounds for dismissal", which other grounds are unspecified. Iowa Electric submits that the railroads have chosen to file a Motion to Dismiss based upon the pleadings.[1/] The railroads have submitted no supporting Verified Statements. Therefore, the Motion should be decided on the pleadings and the averments of the complaint taken as true. On such basis the Motion must be dismissed.

In any event, the procedure suggested by the defendants, to the extnt it would implicitly deny complainant any right to discovery on any issue, including the market dominance issue prior to decision on the jurisdictional question, is totally improper and unreasonable. Similarly, the defendants proposal that they alone should be given an opportunity to pursue discovery related to the market dominance issue is unreasonable. Iowa Electric does not object to a preliminary determination of the jurisdictional market dominance issue, prior to proceeding to a decision on the merits of the reasonableness issue.

[1/] While the railroads make reference to Rule 12(b) of the Federal Rules of Civil Procedure, the Motion is more in the nature of a motion for summary judgment on the pleadings under Rule 12(c), even though the railroads have submitted no Verified Statements.

Iowa Electric's Response To Questions Raised In The Commission's Notice of Policies For Handling Section 229 Cases

In responding to the questions posed in the Commission's Notice to Defendants in this proceeding, Iowa Electric first notes that the railroads have not filed an answer to the complaint as specifically requested and suggested in the Commission's Notice of Policies for Handling Section 229 Cases, served April 28, 1981. Iowa Electric provides the following responses to the indicated questions:

> Q. Is informal settlement contemplated? If so, have negotiations begun and what effect will or should they have on the procedural handling of the case?

Iowa Electric, like the defendants, is ready and willing to discuss any proposed informal settlement. At this time, no settlement proposals have been tendered and no settlement negotiations have begun. It is not anticipated that if any such discussions are begun they would have any immediate effect on the procedural handling of the case.

> Q. Would some form of pre-hearing conference (e.g., meeting in Washington, D.C. or conference phone call) presided over by an Administrative Law Judge assist in resolving the dispute? If so, what procedure is desired?

It is not anticipated that a pre-hearing conference will be of assistance at this time.

> Q. Is there a need for discovery, oral hearing (See Rule 51), staggered deadlines for filing, postponement of evidence taking to allow settlement negotiations, or other special procedures?

Iowa Electric anticipates that extensive discovery will be necessary in the areas of the market dominance issue, the cost of service including operating characteristics and costs incurred by the carriers involved in transporting the coal at issue, and possibly other issues. As indicated above, Iowa Electric objects to the procedure proposed by the railroads for the handling of the market dominance issue in terms of the availability of discovery, although Iowa Electric does not object to having the market dominance issue decided first before the presentation of all evidence on the merits as to reasonableness of the rates involved.

Iowa Electric will require and requests the opportunity to conduct discovery with respect to the market dominance issue prior to the submission of its evidence on that issue. Iowa Electric also will conduct discovery on the merits related to rate reasonableness including the cost of service. In that regard, Iowa Electric may require discovery with respect to the variable cost of service on the market dominance issue if the railroads present evidence, or express their present intention to present such evidence, contending that the ratio of rate to variable cost is less than the threshold jurisdictional level under the Staggers Act.

Iowa Electric recommends that the modified procedure be used in this proceeding. It is not anticipated that there should be any postponement of evidence taking to allow settlement negotiations.

Q. Should other related complaints be consolidated? If so, provide the numbers and titles.

Iowa Electric is aware of no other complaints that raise the same or comparable issues with respect to other movements similar to those that are at issue in any pending complaint. Therefore, there is no need or justification for consolidation of this complaint with any other cases.

Conclusion

In accordance with the foregoing, the Commission is respectfully requested to deny the railroads' Motion to Dismiss. The Commission should also provide for discovery by the complainant prior to the submission of any evidence on the issue of market dominance. Iowa Electric agrees with the railroads that the market dominance issue can be considered and decided first, prior to discovery and the presentation of evidence on the merits as to the issue of reasonableness. The modified procedure should be used in this case.

Dated at Washington, D.C. this 13th day of August, 1981.

Respectfully submitted,

Iowa Electric Light and Power
Company

Of Counsel:

DONELAN, CLEARY,
WOOD & MASER, P.C.
Washington Building
Washington, D.C. 200005

By: John M. Cleary
Nicholas J. DiMichael
DONELAN, CLEARY, WOOD
& MASER, P.C.
914 Washington Building
Washington, D.C. 20005
(202) 783-1215

Attorneys

Dated: August 13, 1981

Due Date: August 13, 1981

Certificate of Service

I hereby certify that a copy of the foregoing Complaint has been served on all parties of record to this proceeding by mailing a copy to them via first-class mail, postage prepaid, on this 13th day of August, 1981.

JOHN M. CLEARY

Senator GRASSLEY. Mr. Stoll.

STATEMENT OF DEAN F. STOLL

Mr. STOLL. Thank you very much, Senator. IPS appreciates this opportunity. I won't read my statement. I'm going to highlight some of the areas in it.

Iowa Public Service Co. provides electricity to approximately 157,000 customers in 228 Iowa and 5 South Dakota communities. We operate 4 coal-fired generating units in the western part of the State, known as Neal Units 1 through 4. We have an interest in some of the other joint-owned plants in Iowa; however, we are only responsible for the coal that moves into Neal station, and that is approximately 3 million tons per year.

We at IPS have no desire to reregulate the railroads. It is also not our goal to revamp the antitrust laws, as S. 447, the subject of today's hearing, would require. Rather, it is our position that the Interstate Commerce Commission could have struck an equitable balance between railroad and captive shippers, under the framework of the Staggers Act of 1980. The ICC has shown little, if any, inclination to strike such a balance. Since our desire is not to reregulate the railroads and not to revamp the antitrust laws, we find ourselves before you today, urging an alternative course of action to S. 447. That alternative is a Consumer Rail Equity Act (S. 477). We feel S. 477 speaks to the question of rail transportation rates in terms of fine tuning, rather than in terms of reregulation or major antitrust revision.

As a matter of specific information on Iowa Public Service Co. in our interest, we have had a rate case before the Interstate Commerce Commission since 1978, a period of 7 years, without resolution to date. That rate case is for movement of coal into Neal Unit No. 4, and we are presently moving coal under another agreement, a pre-Staggers agreement, into Neal Units 1, 2, and 3. The present tariff rate on that agreement is $10.06 per ton. Under the tariff that's being tried to the ICC, we're paying $14.03 per ton, $4 difference, for almost an identical unit, as far as mileage is concerned. One is from Hannah Basin, and one is from the Powder River Basin. The additional cost is $8 million a year for the electric consumers for the electricity generated by Neal Unit No. 4.

I appreciate the opportunity to talk to you, and I stand ready to answer any questions.

[Prepared statement follows:]

STATEMENT OF

IOWA PUBLIC SERVICE COMPANY

BEFORE

UNITED STATES SENATE - COMMITTEE ON THE JUDICIARY

PREPARED BY

DEAN F. STOLL
MANAGER OF FUEL SUPPLY
IOWA PUBLIC SERVICE COMPANY

Iowa Public Service Company (IPS) appreciates this opportunity to provide information and to discuss Rail Transportation Developments.

IPS provides electricity to 157,380 customers in 228 Iowa and 5 South Dakota communities. The Company operates 4 coal-fired generating units, Neal 1, 2, 3 and 4, located south of Sioux City, Iowa, along the Missouri River. IPS also owns 18.5% of the Ottumwa Generating Station, a 675 megawatt coal-fired station located near Chillicothe, Iowa, and 14.5% of the Louisa Generating Station, a 650 megawatt coal-fired electric generating unit located near Muscatine, Iowa.

IPS has direct responsibility for the delivery of coal to Neal Units 1, 2, 3 and 4. The Ottumwa and Louisa units are operated by Iowa Southern Utilities Company, and Iowa-Illinois Gas and Electric Company, respectively. These companies have the primary responsibility for the delivery of coal to these units. All of the units are coal-fired.

All of the coal to Neal Units 1, 2, 3 and 4, as well as Ottumwa and Louisa, is delivered by rail. Neal Units 1, 2, 3 and 4 use approximately 3 million tons of coal per year.

In view of this substantial coal use, all of which is delivered by rail, IPS and its customers, as well as the customers of other joint owners of Neal Units 3 and 4, have a very distinct interest in rail transportation developments and any proposed reforms.

We at IPS have no desire to reregulate the railroads. It is also not our goal to revamp the anti-trust laws as S-447, the subject of today's hearing, would require. Rather, it is our position that the Interstate Commerce Commission (ICC) could have struck an equitable balance between railroad and captive shipper under the framework of the Staggers Rail Act of 1980. The ICC has shown little, if any, inclination to strike such an equitable balance. Since our desire is not to reregulate the railroads and not to revamp the anti-trust laws, we find ourselves before you today urging an alternate course of action to S-447. The alternate we urge is the Consumer Rail Equity Act (S-477). We feel S-477 speaks to the question of rail transportation rates in terms of fine tuning, rather than in terms of reregulation or major anti-trust revision.

All of the coal into the Neal units is delivered by the Chicago and Northwestern Railroad. No other railroad has access to the unloading facilities at those units.

IPS has a specific interest in amending the Staggers Act of 1980 to include added protection for captive shippers due to major problems with the process at the ICC. IPS has been waiting for final conclusion of our Neal 4 rate case since 1978, a period of seven years.

IPS participated in a study by the Department of Energy titled, "Effects of Railroad Regulatory Reform on Coal and Electricity". While the study appeared to be reasonable, there were problems with the conclusions reached in the report. Attached for your information is a copy of a study prepared by the Edison Electric Institute entitled, "Analysis of the Profitability of Rail Rates to Electric Utilities Surveyed in the Draft DOE Report, The Effects of Railroad Regulatory Reform on Coal and Electricity". You should note in that report the pretax return on investment of 93% to the Burlington Northern Railroad (BN) for 1984 on the Neal 4 coal movement as compared to an overall return for the BN of 16% on all rail traffic.

Also included for your information is a news release dated July 22, 1985 from the Edison Electric Institute along with two July, 1985 studies, one titled, "1984 Revenue Adequacy in the Major Coal Hauling Railroads", the other "Railroad Capital Shortfall--Or Surplus?".

All of these reports have been prepared, using methodology that would allow for the determination of revenue adequacy for the railroads in the same way that revenue is calculated for the electric utility industry by the various regulatory agencies. They are intended to explain the differences between the methodology of the Interstate Commerce Commission and the various regulatory bodies that regulate utilities, such as the Iowa State Commerce Commission.

IPS is specifically interested in the areas of determination of market dominance, rate reasonableness, and revenue adequacy. In order to have the Interstate Commerce Commission review a rail rate, it is necessary that a determination be made that a railroad has market dominance. The determination test needs to be reasonable. In regard to rate reasonableness, a standard must be established that protects the truly captive shipper from excessive rates. We feel that there should be a basis to equitably allocate the burden of producing adequate revenues among all captive traffic. In regard to revenue adequacy, we feel that the determination should be made using reasonable accounting standards applied to a reasonable investment base.

As a matter of comparison, we have two rail tariffs under which we move coal into the Neal Complex south of Sioux City. One of those tariffs was negotiated in 1972 at a time when there was a competitive market for the transportation of coal. The present rate being paid under that tariff is $10.03 per ton as of August 1, 1985. The other rate, which is the one that has been before the ICC since 1978, is for the movement of coal into Neal Unit 4. The length of the movement is almost identical. However, the current rate for that movement is $14.03 per ton. We move approximately two million tons of coal per year under the higher rate. Electric consumers pay an additional $8,000,000 per year for electricity generated by Neal 4 due to the higher rate.

Thank you for this opportunity to explain Iowa Public Service Company's position and to furnish you with the enclosed information.

We stand ready to discuss our position further or to review any additional information.

attachments: "The Effects Of Railroad Regulatory Reform On Coal and Electricity"

Edison Electric Institute - News Release

"1984 Revenue Adequacy And The Major Coal-Hauling Railroads"

"Railroad Capital Shortfall--Or Surplus"

Analysis of The Profitability of Rail Rates to Electric Utilities Surveyed in the Draft DOE Report The Effects of Railroad Regulatory Reform on Coal and Electricity

As part of their analysis of the effects of partial rail deregulation on the electric utility industry, DOE examined the circumstances of nine electric utilities with captive coal traffic. DOE claims to have found no evidence of monopolistic pricing on the part of railroads. Rather, its report concluded that:

(a) The problems with the ICC regulatory process are prospective and pose no immediate concern to captive shippers; and

(b) There is no evidence of widespread "abuse" of rates charged to captive shippers by railroads.

Edison Electric Institute (EEI) takes exception to these conclusions. The captive utility coal movements reviewed by DOE provided railroads with a pre-tax return on investment eight times larger than the railroads' average return. Specific pre-tax returns earned on the captive movements ranged from 51 to 148 percent. The railroads have obviously taken advantage of their monopoly power to earn such large returns.

For many years, utilities and other shippers have been active participants in the regulatory and administrative process at the ICC. These efforts have proved unsuccessful in securing effective protection for captive traffic. The resultant public record contains ample evidence of monopolistic pricing practices by railroads over captive shippers and documents the failure of the ICC's regulatory process to provide the necessary "back up regulation."

DOE's conclusion that railroads have not imposed "abusive" rates on captive shippers is based on the observation that, since the enactment of the Staggers Rail Act in 1980, annual increases in rail rates have not significantly exceeded the inflation rate. The DOE approach is faulty since it fails to consider:

- the relation between the cost of providing the service and the rates charged;
- whether the rates were reasonable when first established;
- that many of these rates increased substantially just prior to the time period which DOE reviewed.

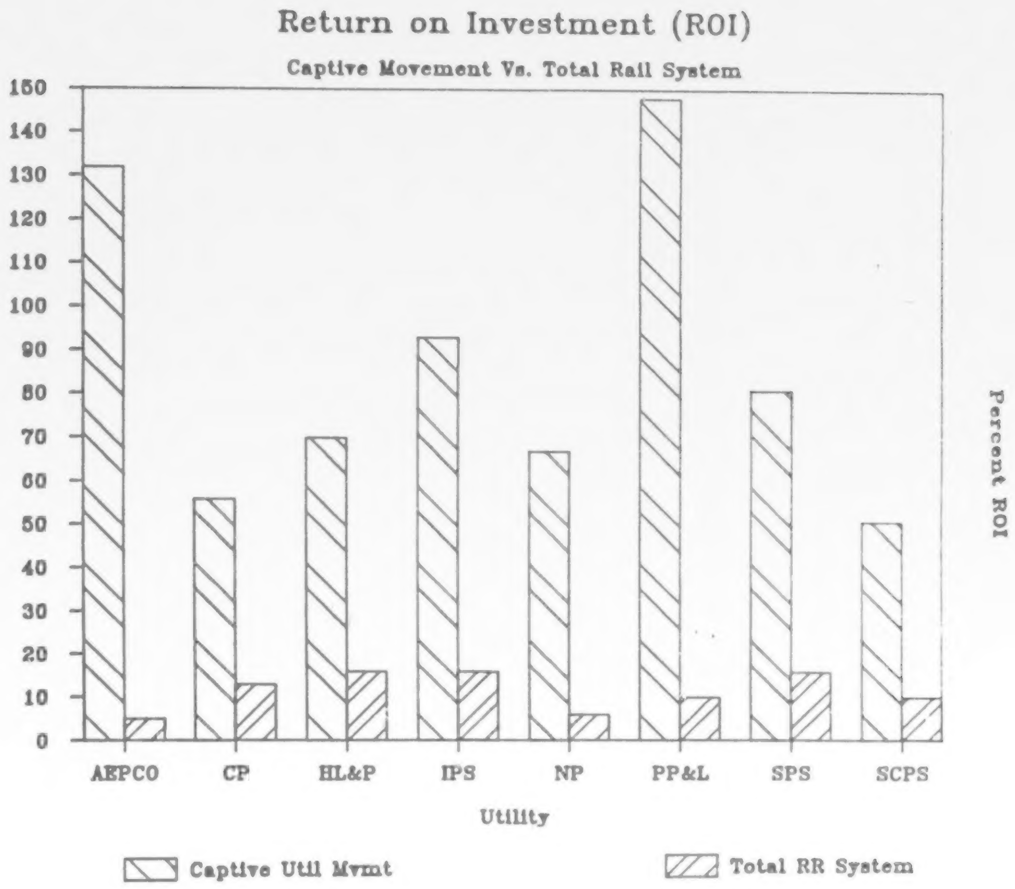
DOE's focus only on rate increases since 1980, does not tell the whole story. A more direct approach is to determine the profitability of each captive movement. One way to do so, is to measure a railroad's return on the investment used in providing the service to each captive shipper. This is calculated as net revenues (revenues less costs) over investment. Using these return on investment calculations, it is possible to make a relative comparison of the profitability generated by individual utility coal movements with the overall profitability of the whole railroad system.

The information necessary to calculate the return on investment employed in providing rail service is contained in testimony filed in individual ICC rate proceedings and was submitted to DOE by the respondent utilities.

EEI's analysis is based on the same information that was provided to DOE. The table and graph below compare the pre-tax return on investment employed in utility rail service with the total return on railroad investment. For the respondent utilities, the pre-tax return on investment employed in coal traffic is, on average, eight times greater than the return earned on total railroad investment. The magnitude of the pre-tax return on investment from these captive movements substantiates the fact that railroads have engaged in monopoly pricing on their captive coal traffic. Additional details are contained in the attached utility case summaries.

		Pre-Tax Return on Investment (1984)	
Company	Railroad	Captive Utility Coal Movement	All Rail Traffic(ICC)
Arizona Elec Power Co-op	Sante Fe	132%	5% *
Consumers Power	C&O	56%	13%
Houston Lighting & Power	BN	70%	16%
Iowa Public Service	BN	93%	16%
Nevada Power	UP	67%	6%
Pennsylvania Power & Light	Conrail	148%	10%
Southwestern Public Service	BN	81%	16%
South Carolina Public Service Authority	SCL	51%	10%

*1983 Basis - 1984 data not available



Return on Investment (ROI)
Captive Movement Vs. Total Rail System
Percent ROI
150
140
130
120
110
100
90
80
70
60
50
40
30
20
10
0
AEPCO
CP
HL&P
IPS
NP
PP&L
SPS
SCPS
Utility
Captive Util Mvmt
Total RR System

KEY CONGRESSIONAL SPONSORS
S. 477/H.R. 1190

The Honorable Mark Andrews
United States Senate
724 Senate Hart Office Building
Washington, D.C. 20510

The Honorable Russell B. Long
United States Senate
225 Senate Russell Office Building
Washington, D.C. 20510

The Honorable Wendell Ford
United States Senate
173A Senate Russell Office Building
Washington, D.C. 20510

The Honorable Ted Stevens
United States Senate
522 Senate Hart Office Building
Washington, D.C. 20510

The Honorable Billy Tauzin
United States House of Representatives
222 Cannon House Office Building
Washington, D.C. 20515

The Honorable Harold Rogers
United States House of Representatives
206 Cannon House Office Building
Washington, D.C. 20515

The Honorable Nick Rahall
United States House of Representatives
343 Cannon House Office Building
Washington, D.C. 20515

EDISON ELECTRIC INSTITUTE The association of electric companies
1111 19th Street, N.W.
Washington, DC 20036

June 14, 1985

Attachment 5

NEWS

EDISON ELECTRIC INSTITUTE The association of electric companies
1111 19th Street, N.W.
Washington, D.C. 20036-[illegible]

FOR ADDITIONAL INFORMATION CONTACT:
Gloria Dittus or Tony Anthony
202-828-7582 or 800-424-8897

FOR IMMEDIATE RELEASE
Monday, July 22, 1985

Contradicts ICC Analysis

STUDY FINDS TOP COAL-HAULING RAILROADS EXCEED REVENUE ADEQUACY BY $800 MILLION IN 1984

WASHINGTON (July 22) -- A study prepared by the Edison Electric Institute (EEI) and endorsed by the National Association of Regulatory Utility Commissioners (NARUC) finds that the nation's five largest coal hauling railroads exceeded revenue adequacy needs by approximately $800 million in 1984.

The study used analytical and accounting standards recommended by NARUC, which represents regulators in all 50 states as well as federal agencies. Railroad rates for captive coal shipments are under the jurisdiction of the Interstate Commerce Commission.

Edward F. Mitchell, president of Potomac Electric Power Co. and chairman of Consumers United for Rail Equity presented the findings. D.C. Public Service Commissioner Wesley Long, who serves on NARUC's Electricity Committee, endorsed the report's methodology.

"The question of whether the railroads are 'revenue adequate' is crucial to the current debate over the reasonableness of railroad charges for hauling captive coal. The Interstate Commerce Commission (ICC), using its own methodolgy, gives revenue inadequate railroads essentially free reign in raising rates to captive shippers," Mitchell said at a press briefing here today.

The ICC has taken the position that as long as a railroad is revenue "inadequate" then no captive shipper rate is unreasonable -- unless it exceeds "stand alone cost", i.e. what it would cost a shipper to build and operate it's own railroad. Since 1981, the ICC has found all major railroads to be "revenue inadequate" despite the fact that the major coal hauling railroads have enjoyed $13 billion in surplus funds from operations since 1976 according to an EEI study.

This surplus is the difference between internally-generated funds (after dividends, depreciation, and tax payments) and capital expenditures. "Clearly, such financial performance strongly suggests that these railroads are not revenue inadequate," Mitchell said.

Long stressed, "The method the ICC uses to determine railroad revenue adequacy is simply not consistent with the practices generally used by other regulatory agencies. The ICC's approach overstates the railroad's investment base, cost of capital, and level of expenses, while understating railroad income."

Recognizing that the ICC's methodology and procedures are significantly different, NARUC, in 1984, passed a resolution in support of legislative changes which would bring the ICC revenue adequacy methodology in line with the methodology applied by other regulatory agencies.

"By comparing the current ICC methodology with the approaches recommended by NARUC, a substantially improved picture of railroad financial health develops," Long said. "Put simply, the ICC significantly overstates railroad revenue requirements. This overstatement would increase even further under the pending ICC proposal to apply replacement cost accounting," Long said.

The railroads studied were the Burlington Northern, Norfolk Southern, Chesapeake and Ohio, Missouri Pacific, and Seaboard System which collectively account for approximately 75 percent of all originated coal traffic. By applying the NARUC supported methodology to determine revenue adequacy for 1984, the Burlington Northern was found to have a $400 million surplus as compared with a calculated shortfall of $500 million under the ICC methodology; the Norfolk Southern, a $400 million surplus compared to a $500 million shortfall; the Chesapeake & Ohio a surplus of $100 million contrasted with a shortfall of $300 million; the Missouri Pacific was found to have no shortfall as opposed to a $600 million deficit; and Seaboard System to have a $100 million shortfall instead of the $600 million shortfall.

The coal-rail debate centers around efforts to amend the Staggers Rail Act of 1980 which eliminated regulation of rates for competitive rail traffic. Congress recognized, however, that for "captive" traffic where no effective competition exists, regulatory protection from railroad monopoly power was necessary. The Staggers Act directed the ICC to recognize the national interest in a healthy railroad system while implementing a national policy to assure rates to "captive" traffic are "reasonable."

"Captive shippers have consistently testified that the ICC's process for determining revenue adequacy is seriously flawed and does not reflect the true financial condition of the railroads," Mitchell said.

"Until the ICC begins to analyze railroad financial data in the same fashion as other regulatory agencies this nation's electricity consumers will continue to be faced with unnecessarily high transportation rates," according to Long.

"The only recourse consumers and captive shippers have is through a legislative solution. Since the ICC is on record stating that they will not change their determination of railroad revenue adequacy, Congress must act. The Consumer Rail Equity Act must be passed," Long said.

"Captive shippers are being held hostage by an inadequate and unreasonably burdensome regulatory system. In effect, the ICC has constructed regulatory hoops and hurdles which, even if successfully completed, are rendered irrelevant because of the ICC's unreasonable definition of revenue adequacy," Mitchell added.

"Passage of the Consumer Rail Equity Act remains the only viable solution," Mitchell concluded.

# # #

JULY, 1985

1984 REVENUE ADEQUACY
AND
THE MAJOR COAL-HAULING RAILROADS

Introduction

A key factor in the Interstate Commerce Commission (ICC) determination of the reasonableness of rail rates for captive shippers is whether or not the ICC has found the railroad to be "revenue adequate." If the ICC finds a railroad is not revenue adequate (and it has found all major railroads to be "inadequate" since 1981), the railroad is granted additional ratemaking freedoms. These freedoms have been applied by the ICC in such a manner that, since the passage of the Staggers Rail Act of 1980, no captive rail coal rate has been found to be unreasonable, no matter how high.

Captive shippers have testified before the ICC on numerous occasions that the ICC's process for determining revenue adequacy is seriously flawed and does not reflect the true financial condition of the railroads, especially the major coal-hauling carriers. The ICC's computation of revenue adequacy is performed in a manner which is not consistent with the practices generally used by other regulatory agencies. The ICC's approach overstates the railroad's investment base, cost of capital, and level of expenses, while understating railroad income. Furthermore, the ICC revenue adequacy determination is based on data that the ICC and the railroads acknowledge contain "material" errors. As a result, the ICC's revenue adequacy determinations consistently understate the financial condition of the railroads.

The railroad industry has argued that it is evaluated by the same financial criteria, return on investment (ROI) and cost of capital, as regulated electric utilities. Although the names of the criteria may be the same, the overall methodology used by the ICC to compute them is not.

The National Association of Regulatory Utility Commissioners (NARUC), representing the state regulatory bodies chargeo with regulating electric, water, gas, telephone, and other business activities, has recognized that the ICC's methodology and procedures are significantly different from those generally followed by other regulatory commissions. In a resolution, released on March 5, 1984, (attached as Appendix A) NARUC expressed support for legislative changes which would bring the ICC revenue adequacy methodology into general conformity with the methodology applied by other regulatory agencies. The changes NARUC urged included the use of:

a. The embedded cost of debt;

b. Standard original cost depreciation accounting;

c. Other measures commonly applied by regulators in calculating the railroad's return on investment; and

d. When appropriate, actual equity and contractual debt costs of a holding company and an analysis of the reasonableness of transfer prices between affiliates.

Applying the approach recommended by NARUC to the 1984 reported financial data for the five major coal-hauling railroads demonstrates that these railroads as a group generated revenues that exceeded their revenue adequacy requirements by approximately $800 million. On the other hand, if the ICC's current methodology is applied, these same railroads would fall short of the ICC's revenue adequacy requirement by $2.4 billion. This shortfall would be considerably increased under the pending Commission proposal to apply replacement cost accounting. The carriers studied (Burlington Northern, Norfolk-Southern, Chesapeake and Ohio, Missouri Pacific, and Seaboard System) collectively account for approximately 75 percent of all originated coal traffic.

	ICC	NARUC
Revenue Requirement	$4.8	$2.3
Reported Income	$2.4	$3.1
Variation from Revenue Adequacy Requirement	($2.4)	$0.8

Note: All figures are pre-tax dollars (billions).

Background

Debates on national rail policy invariably focus on discussions of railroad industry financial health. The ICC maintains that industry profits are substandard. The Association of American Railroads (AAR) agrees with the ICC findings and argues that the investor-owned electric utility industry is considerably more profitable than the rail industry. It claims that all the railroads desire is to achieve the same level of return as the electric utilities.

The ICC's portrayal of railroad financial performance is inaccurate and seriously distorts any analysis of the reasonableness of individual rail rates, and of overall rail rate policy. The ICC has effectively taken the position that revenue inadequate railroads may increase rates to captive shippers until the railroads become revenue adequate. Moreover, the perception that all railroads are revenue inadequate is used to justify the ICC's defacto dismantling of the regulatory system.

Contrary to the image created by the ICC and the AAR, there are many indications that the nation's major coal-hauling railroads are enjoying strong financial health. For example, over the 1976-85 period, the nation's major railroads produced some $13 billion in surplus funds from operations. This surplus is the difference between internally-generated funds (after dividends, depreciation, and tax payments) and capital expenditures (see Appendix C). Clearly, such financial performance strongly suggests that these railroads are not revenue inadequate.

Because these circumstances suggest serious deficiencies in the ICC's approach to revenue adequacy, a comparative analysis (see page 7) was made between the ICC's current methodology and the methodology recommended by NARUC for analyzing financial performance. This analysis relies upon railroad financial reports for 1984 and AAR's estimate of the railroads' 1984 cost of capital as submitted to the ICC in Ex Parte No. 458.

The conceptual differences between these methodologies can be summarized as follows:

- NARUC supports use of historical original cost investment base valuation and depreciation accounting. The ICC, on the other hand, applies an alternative method of accounting, unique to the railroad industry, in all of its revenue adequacy determinations.

- NARUC supports elimination of deferred taxes from the railroad investment base. It is the common practice of all other regulatory bodies to exclude deferred taxes from the investment base or to consider them as funds obtained at zero cost of capital. With either approach, the result is the same--no return is authorized on the deferred tax amount. The ICC, on the other hand, includes these funds in the investment base even though they are acquired at no cost.

- NARUC supports calculation of the cost of capital considering:
    - The contractual cost of debt (as opposed to the current cost);
    - The actual book value of debt and equity (as opposed to a relationship based on market value); and
    - The actual cost of preferred stock (as opposed to including it in common equity).

In addition, other modifications to the ICC's methodology are required to adjust for deficiencies recognized by the ICC and distortions caused by a one-time modification of accounting methodology for track and structures. These modifications are:

- Inclusion of other transportation-related investment, income, and expenses. These adjustments were proposed by the ICC in 1983 in an effort to correct flaws which the ICC acknowledged resulted in "material" errors. However, the ICC has not yet adopted these proposals.

- Adjustment of the investment base. The ICC permitted railroads to "write-up" their investment base during the process of converting their accounting system from Retirement Replacement Betterment (RRB) to

> Depreciation Accounting in 1983. This write-up in assets permitted expenditures, charged against income in prior years, to be added to the investment base and thereby recovered a second time through depreciation charges against income. This practice is contrary to normal regulatory procedure, which uses original cost accounting. To implement this adjustment the overall value of the railroad investment base was reduced by \$3.4 billion, the amount of write-up reported by the railroads in question.

The comparison of the current ICC methodology with the approaches recommended by NARUC produces substantially different depictions of railroad revenue adequacy for the above group of coal-hauling railroads.

- The ICC methodology shows a 1984 investment base for these major coal-hauling railroads of \$19.2 billion. The NARUC approach would show an investment base of \$10.5 billion as a result of:
  - Elimination of deferred taxes of \$5.3 billion; and
  - Elimination of the "write-up" in the investment base of \$3.4 billion due to the capitalization of costs already charged to income.
- The ICC methodology produces an estimated 1984 pre-tax cost of capital of 25.15 percent. The NARUC approach produces a weighted average cost of capital for these major coal-hauling railroads of 22.29 percent.
- The ICC methodology produces a 1984 before tax net income for these major coal-hauling railroads of \$2.4 billion. Adjustments, consistent with the NARUC approach, have been proposed but not yet adopted by the ICC. These adjustments would include other transportation-related income (approximately \$0.8 billion), which would increase the 1984 before tax net income figure to \$3.1 billion.

Conclusion

The ICC shows 1984 pre-tax revenues for the major coal-hauling railroads are \$2.4 billion less than needed to achieve revenue adequacy. In comparison, the approach supported by NARUC produces pre-tax revenues of \$0.8 billion in excess of those needed to achieve revenue adequacy.

A comparison of procedures supported by NARUC with the ICC's current revenue adequacy methodology shows that the ICC significantly overstates railroad revenue requirements. This overstatement would increase even further under the pending Commission proposal to apply replacement cost accounting. The procedures supported by NARUC clearly show that the majority of major coal-hauling railroads were revenue adequate in 1984.

Details of these findings are shown in the following attachments:

Table I	Comparison of Current ICC Revenue Adequacy Methodology with Approach Supported by NARUC for Major Coal-Hauling Railroads--1984
Table II	Comparison of Current ICC Revenue Adequacy Methodology with Approach Supported by NARUC for Individual Major Coal-Hauling Railroads--1984
Table III	Investment Base Write-Up Reported by Railroads Resulting from Change from Retirement Replacement Betterment (RRB) to Depreciation Accounting in 1983
Appendix A	NARUC Resolution
Appendix B	Study Methodology
Appendix B(1)	Determination of 1984 Cost of Capital-ICC Methodology
Appendix B(2)	Determination of 1984 Cost of Capital-NARUC Supported Approach
Appendix B(3)	Adjustments to Investment Base and Income Statement (Proposed by ICC)
Appendix B(4)	Elimination of 1983 Investment Base Write-up
Appendix B(5)	Elimination of Deferred Taxes from Investment Base
Appendix C	Summary Analysis of DOT Railroad Shortfall Study

Table I

Comparison of Current ICC Revenue Adequacy Methodology
with Approach Supported by NARUC for
Major Coal-Hauling Railroads (1)--1984

(Before Tax Dollars in Billions)

		ICC	NARUC	
1.	Investment Base	$19.2	$10.5	(2)
2.	Cost of Capital	25.15%	22.29%	(3)
3.	Required Return (L. 1 x L. 2)	$4.8	$2.3	
4.	Reported Income	$2.4	$3.1	(4)
5.	Revenue (Shortfall)/Surplus (L. 4 minus L. 3)	($2.4)	$0.8	

(1) BN, NS, C&O, MP and SBD.

(2) Excludes deferred taxes (less investment tax credits); includes other transportation-related investment, adjustment for 1983 write-up in rail assets.

(3) Weighted average of individual carriers.

(4) Includes other transportation-related income and expense.

Source: AAR 1984 Cost of Capital submittal to ICC
Railroad 1984 financial reports to ICC.

Table II

Comparison of Current ICC Revenue Adequacy Methodology with Approach Supported by NARUC for Individual Major Coal-Hauling Railroads--1984

(Before Tax Dollars in Billions)

Railroad	Revenue Requirements		Reported Income		(Shortfall)/ Surplus	
	ICC	NARUC	ICC	NARUC	ICC	NARUC
Burlington Northern	$ 1.5	$ 0.8	$ 0.9	$ 1.1	$(0.5)	$ 0.4
Norfolk Southern	1.2	0.6	0.7	1.0	(0.5)	0.4
Chesapeake & Ohio	0.4	0.2	0.2	0.3	(0.3)	0.1
Missouri Pacific	0.7	0.3	0.2	0.3	(0.6)	0.0
Seaboard	0.9	0.6	0.3	0.5	(0.6)	(0.1)
Total	$4.8	$2.3	$2.4	$3.1	($2.4)	$0.8

Note: Numbers may not add due to rounding.

Source: AAR 1984 Cost of Capital submittal to ICC In Ex Parte No. 458.

Railroad 1984 financial reports to ICC.

Table III

Investment Base Write-Up Reported by Railroads Resulting from Change from Retirement Replacement Betterment (RRB) to Depreciation Accounting in 1983

(Billions of Dollars)

	Average Net Investment		
Railroad	RRB	Depreciation	Write Up
Burlington Northern	$4.188	$5.427	$1.239
Chesapeake & Ohio	1.213	1.487	.274
Missouri Pacific	2.555	2.764	.209
Seaboard	3.153	3.708	.555
Norfolk & Western	2.331	2.664	.333
Southern	2.721	3.530	.809
Total	$16.161	$19.580	$3.419

Average percent net investment write up 21%

Source: AAR Analysis of Class I Railroads--1983.

APPENDIX A

NARUC News

NATIONAL
ASSOCIATION
OF
REGULATORY
UTILITY
COMMISSIONERS

1102 I.C.C. Building • P.O. Box 684 • Washington, D. C. 20044 • Telephone 202/628-7324

FOR IMMEDIATE RELEASE No. 22-84

CONTACT: Linda Kent 5 March 1984

STATE REGULATORS URGE CONGRESS TO PROVIDE REASONABLE RATES FOR CAPTIVE RAILROAD TRAFFIC AND TO PROVIDE SHIPPERS ACCESS TO RAILROAD FACILITIES

Washington, D.C.----Objecting to recent Interstate Commerce Commission (ICC) decisions regarding the pricing of captive railroad traffic, the policy-making body of the National Association of Regulatory Utility Commissioners (NARUC) adopted a resolution urging Congress to "ensure reasonable rail rates for captive rail traffic" and to permit shippers access and usage of railroad facilities.

Meeting here February 29 and March 1, the NARUC's Executive Committee approved the resolution regarding the ICC's implementation of the Staggers Rail Act sponsored by the Association's Committee on Electricity.

Specifically, the NARUC resolution records its objections to ICC decisions which define "market dominance" so as to place ICC regulatory protection beyond the reach of many captive coal shippers; set standards for "reasonable" rates which have no relation to the cost of providing service and will allow those rates to double; exempt export coal from regulation; and define "revenue adequacy" unrealistically so that no Class I railroads are considered to have adequate revenues.

The NARUC also objected to the ICC's usurpation of State authority to regulate intrastate railroad traffic.

The resolution expresses the concern of the Association that, because over half of the electricity in the U.S. is generated by coal and the majority of the coal is transported to electric utilities under non-competitive conditions, the customers of electric utilities will unnecessarily incur much higher electricity rates as a result of the ICC determinations.

The NARUC resolution calls on Congress to enact legislation to:

- define "market dominance in the context of effective competition;

- require the use of embedded cost of debt. standard original cost depreciation accounting. other measures commonly applied by regulators in calculating return on investment. and when appropriate to consider equity and debt costs to the holding company and the reasonableness of the transfer price in determining revenue adequacy;

- require ICC consideration of the cost to the railroad of providing service. whether the traffic involved is paying an unreasonable share of the railroad's fixed costs. the impact of the rate on national energy goals. the extent to which railroad revenue shortfalls are attributable to hauling traffic at noncompensatory rates or failing to maximize earnings on competitive traffic. and price stability and impact on shippers in setting maximum reasonable rates;

- require the ICC to calculate the inflation index upon which automatic rate increases are based on the basis of actual. not imputed increases in costs;

- reauthorize and fund the Railroad Accounting Principles Board;

- adopt fair and reasonable procedures for ICC review of State regulatory decisions;

- prevent anticompetitive or predatory cancellations of joint rates;

- prohibit the ICC from exempting market dominant traffic;

- require rail carriers to permit access and usage of facilities to shippers; and.

- review line abandonment procedures to ensure against abandonment of rail services due to the operational preferences of the rail companies.

The text of the resolution follows:

Resolution Adopted by
the National Association of Regulatory Utility Commissioners

RESOLUTION

To Provide Reasonable Rates for Captive Railroad Traffic Under Standards Consistent with and Similar to Those Generally Applied by State Regulatory Commissions

AND

To Provide Shippers Access and Use of a Railroad's Facilities

WHEREAS. the Staggers Rail Act of 1980 provided for the deregulation of competitive rail traffic and directed the Interstate Commerce Commission to continue to maintain reasonable rates where there is an absence of effective competition for rail traffic within the Commission's jurisdiction; and

WHEREAS. over half of the electric energy in the United States is generated using coal. the majority of which is transported to electric utilities under non-competitive conditions by one railroad and subject to the jurisdiction of the Interstate Commerce Commission; and

WHEREAS. the Interstate Commerce Commission has issued a series of decisions effectively withdrawing regulation over the pricing of this captive rail traffic, including decisions which: (1) define "market dominance" so as to place ICC regulatory protection beyond the reach of many captive coal shippers; (2) set standards for "reasonable" rates which have no relation to the cost of providing service and which will allow coal transportation rates to double in real terms in five years; (3) exempt export coal from regulation although United States coal is already fifteen to twenty percent more costly than world market prices due in large part to transportation costs; (4) define "revenue adequacy." on which several pricing freedoms for railroads under the Staggers Act are based. unrealistically. so that no Class I railroads. no matter how profitable. are considered to have adequate revenues. and highly profitable railroads will be allowed billions of dollars in extra rate increases; and

WHEREAS. customers of electric utilities will. unnecessarily. incur much higher electricity rates as a result of these ICC determinations; and

WHEREAS. over the repeated objections of NARUC and individual State commissions. the Interstate Commerce Commission has usurped State authority to regulate intrastate railroad movements consistent with the Staggers Act; and

WHEREAS. the railroad industry. consumers and the captive shippers that serve them would benefit from (1) the restoration of competition to rail service areas now served by only one railroad and (2) the assurance that fair and reasonable freight rates are charged;

NOW, THEREFORE. BE IT RESOLVED that the National Association of Regulatory Utility Commissioners assembled at Washington. D.C. on March 1. 1984 urges Congress to enact legislation.

First to ensure reasonable rail rates for captive rail traffic. including provisions which:

1. Define "market dominance" in the context of effective competition for the transportation to which the rate applies. so that all captive shippers may obtain ICC regulatory review;

2. Require consideration. in determining "adequate revenues" for railroads. of several realistic indicators of financial health. and require:

   a. the use of embedded cost of debt.,

   b. standard original cost depreciation accounting.

   c. other measures commonly applied by regulators in calculating the railroad's return on investment. and

   d. when appropriate. consider equity and debt costs to the holding company and look at the reasonableness of the transfer price between affiliates;

3. Require ICC consideration. in setting maximum reasonable rates. of the following standards:

   a. the cost to the railroad of providing the service involved;

   b. whether the traffic involved is paying an unreasonable share of the railroad's fixed costs;

c. the impact of the rate on national energy goals;

d. the extent to which railroad revenue shortfalls are attributable to hauling traffic at noncompensatory rate levels or failing to maximize earnings on competitive traffic; and

e. price stability and impact on shippers;

4. Require the ICC to calculate the inflation index (as set forth in the Interstate Commerce Act) upon which automatic rate increases are based on the basis of actual. not imputed. increases in costs; as well as allowances for productivity gains; and to require rail rates which have increased automatically with that inflation index to decrease when decreases in railroad costs lower that index;

5. Reauthorize and fund the Railroad Accounting Principles Board;

6. Require adoption of fair and reasonable procedures for ICC review of State regulatory decisions on intrastate rail rates;

7. Prevent anticompetitive or predatory cancellations of joint rates;

8. Prohibit the Interstate Commerce commission from exempting market dominant traffic from regulation; and

9. Prohibit the use of confidential pricing in shipping contracts. but in contrast make available all information necessary to ensure enforcement of (Long-Cannon) Congressional intent against cross subsidy; and

Second to require:

a. rail carriers to permit. with reasonable compensation. access and usage of facilities to shippers for whom the sole means of connecting with the trackage of another rail carrier or of reaching the destination of a shipment is over the railroad's facility; and

b. a review of line abandonment procedures to ensure against abandonment of rail service due to the operational preferences and/or strategic planning of the rail companies;

BE IT FURTHER RESOLVED that the National Association of Regulatory Utility Commissioners supports legislative initiatives to address these critical issues. and urges the Congress to enact legislation to obtain for captive rail shippers

1. protection from the practices outlined above. and

2. access to competitive rail service and to obtain for consumers fair and reasonable regulation which protects them from exploitation.

# # #

Founded in 1889. the NARUC is a quasi-governmental. nonprofit organization whose members include regulatory bodies of the fifty States. the District of Columbia. Puerto Rico and the Virgin Islands. Designed to serve the public interest by seeking to improve the quality and effectiveness of government regulation of carriers and utilities. its members play a crucial role in shaping the profile and substance of public regulation in America today.

APPENDIX B

Study Methodology

The analysis consisted of a comparison of the results of applying the current ICC methodology for determining revenue adequacy versus the results of applying procedures supported by NARUC.

The study developed the revenue requirements for the selected railroads and contrasted it with their reported income under each of the above methodologies .

The differences between the ICC methodology and the NARUC supported approach are explained in Appendices B(1) through B(5).

APPENDIX B(1)

Determination of The 1984 Cost of Capital-ICC Methodology

Each year, the ICC institutes a proceeding to collect data for the determination of the prior year's railroad industry average cost of capital. Data used in this determination includes:

- Return on Shareholder Equity (After Tax)
- Cost of Debt (Current)
- Debt Equity Ratio (Market Value)

The primary source of railroad industry data is the Association of American Railroads (AAR). Although any party may submit their own data and comments, the Commission has generally accepted the AAR data, with some adjustments, for use in the cost of capital calculation. In recent years, the Commission has adjusted the AAR's data, reducing the return on shareholder equity number submitted by the AAR.

Once determined, the cost of capital becomes the standard by which the ICC judges the retrospective revenue adequacy of each Class I railroad.

Although the Commission has not completed a 1984 cost of capital proceeding, the AAR has already submitted its 1984 industry data. Applying the adjustment to the return on shareholder equity which the Commission has used in prior cost of capital proceedings, and using the balance of the AAR data, it was possible to calculate a reasonable approximation of what the ICC would determine as the 1984 railroad cost of capital.

The calculation is as follows:

$$\begin{aligned} & (\text{Cost of Shareholder Equity}) \times \left(\frac{\text{\% Equity}}{100}\right) \\ \text{plus} \quad & (\text{Cost of Debt}) \times \left(\frac{\text{\% Debt}}{100}\right) = \text{Weighted Cost of Capital} \end{aligned}$$

Substituting Values Yields:

$$[(17.0) \times (.661)] + [(12.8) \times (.339)]$$

$= \underline{15.57}$ percent after tax cost of capital.

The ICC, in applying the cost of capital in its regulatory proceedings, uses the above figure on a before tax basis. The assumption made by the ICC is that the statutory tax rate of 46% is paid by the rail carriers. This yields a before tax cost of equity of $\underline{31.48}$% [17.0 ÷ (1.0 - .46)]. The before tax cost of capital is $\underline{25.15}$%.

APPENDIX B(2)

Determination of The 1984 Cost of Capital-- NARUC Supported Approach

The major differences between the ICC's methodology for computing the cost of capital and those supported by NARUC center on:

- Use of embedded as opposed to current cost of debt. NARUC supports the use of embedded or actual historical cost of debt being incurred. The ICC, on the other hand applies a current cost of debt to all debt regardless of when it was incurred or at what cost. This results in a significant overstatement of the cost of debt portion of the cost of capital calculation.

- Use of book values for determining the debt equity ratio as opposed to market values. Book values represent the actual amount of outstanding debt and the accounting value of the firm's equity. The ICC's unique method of using market values to determine the debt equity ratio is contrary to commonly accepted regulatory practices. It distorts the true debt equity ratio by placing a greater weighting on the higher cost equity portion. This occurs because the discounted market value of debt is appreciably below the actual debt outstanding on railroad books. This phenomenon arises because interest rates in recent years have been appreciably above the actual contractual interest rate of the debt.

Computing the annual railroad cost of capital using the NARUC supported approach requires the following data:

- Return on shareholder equity (after tax)
- Cost of debt (embedded)
- Cost of preferred stock (after tax)
- Debt-equity ratio (book value)

Computation of the cost of capital, where possible, was made on an individual railroad basis, using individual railroad reported 1984 data, except for the return on shareholder equity and the cost of preferred stock. The return on shareholder equity used was the adjusted industry average number used in determination of the ICC version of cost of capital. No railroad data has been reported on the cost of preferred stock for 1984. Therefore, the cost of preferred stock was conservatively estimated to be one-half percentage point under the AAR's 1984 current industry average cost of debt (12.3%) in line with the general experience of the utility industry.

The calculation is as follows:

$$(\text{Shareholder Equity}) \times \left(\frac{\%\ \text{Equity}}{100}\right)$$

plus $$(\text{Cost of Preferred Stock}) \times \left(\frac{\%\ \text{Preferred}}{100}\right)$$

plus $$(\text{Cost of Embedded Debt}) \times \left(\frac{\%\ \text{Debt}}{100}\right)$$

= Weighted Cost of Capital

APPENDIX B(3)

Adjustments to Investment Base and Income Statement (Proposed by ICC)

In its proceeding, Ex Parte No. 393 (Sub-No. 1), issued on February 18, 1983, the ICC proposed to amend its computation of Return on Investment (ROI) to include the investment, income and expenses related to railroad affiliated operations, i.e., terminal facilities, and interest in other rail operations. The ICC stated that its proposal would "view revenue adequacy in its proper perspective." The current ROI computation includes only data from direct railroad operations.

Using the data reported by railroads in their annual R-1 reports to the ICC, adjustments to the investment base and income statement were made along the guidelines proposed by the Commission in the Ex Parte No. 393 (Sub-No. 1) proceeding.

The forecast $13 to $16 billion "shortfall," as it came to be known, proved to be a key issue in influencing the further deregulation of railroads under the Staggers Rail Act of 1980 (Staggers Act). The projected failure of the railroads to earn sufficient revenues and the implied threat of the necessity for federal bailout was used by railroad industry supporters in their successful effort to pass the Staggers Act. The Congressional Record of the passage of the Staggers Act contains numerous references to the forecast shortfall and other conclusions of the DOT report. The Staggers Act itself, in its findings (Sec. 2(7)), stated that:

> by 1985, there will be a capital shortfall within the railroad industry of between $16,000,000,000 and $20,000,000,000.

The perception of a "shortfall" still exists and the railroad industry continues to use it in support of the argument that their industry remains in dire financial need. Although some supporters acknowledge that the original $13-$16 billion shortfall forecast may not have fully materialized, they still believe some shortfall exits. No one, however, has attempted to document what the financial performance of the railroad industry actually has been. This paper makes that much needed comparative

APPENDIX B(4)

Elimination of 1983 Investment Base "Write-Up"

In its decision, Docket No. 36988, dated January 26, 1983, the ICC directed railroads to change their method of accounting from Replacement, Retirement, Betterment (RRB) to Depreciation Accounting (DA), beginning with calendar year 1983. The basic difference between RRB and DA is the fact that under RRB, expenditures incurred in the replacement of railroad track and structures were expensed against current income, rather than capitalized as normal practice would require. As an expense item charged against income, the cost of the replacement work was fully recovered in the year it was incurred.

The Commission, in directing the change to DA, authorized the railroads to capitalize these already recovered track and structure expense items at the cost of most recent replacement and depreciate them. The net result is that railroads are permitted to recover the cost of these prior track and structure replacements twice. This "write-up" of the investment base, or "double dip", is contrary to practices which would be allowed by all other regulatory agencies.

Because the ICC required the reporting of the railroad investment base for 1983 under both original RRB and DA methods, it was possible to determine the magnitude of the write-up (see Table III). The amount of each railroad's reported write-up was deducted from the 1984 investment base prior to calculating its revenue adequacy using generally accepted regulatory procedures.

APPENDIX B(5)

Elimination of Deferred Taxes from Investment Base

It is the common practice of all other regulatory bodies to exclude deferred taxes from the investment base or to consider them as funds obtained at zero cost of capital. With either approach, the result is the same--no return is authorized on the deferred tax amount.

The revenue adequacy computation according to ICC methodology includes deferred taxes in the investment base. The revenue adequacy calculation following NARUC supported practices excludes deferred taxes from the investment base.

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1111 19th Street, N.W.
Washington, DC 20036

JULY, 1985

APPENDIX C

SUMMARY ANALYSIS OF DOT RAILROAD SHORTFALL STUDY

THE RAILROAD CAPITAL SHORTFALL -- WHAT HAPPENED TO IT?

In October, 1978, the U.S. Department of Transportation (DOT) submitted a report to Congress entitled "A Prospective for Change in the Freight Railroad Industry." The report was prepared in response to the requirements of section 504 and 901 of the Railroad Revitalization and Regulatory Reform Act of 1976 (the 4R Act). The primary purpose of the DOT report was to assess the capital needs of the railroad industry for the period 1976-1985 and determine whether those needs could be met by private sources of capital. In the event the capital requirements could not be met by private sources, an estimate of the financial assistance the federal government should provide was to be made.

The report found that: "requirements for funds by Class I railroads exclusive of Consolidated Rail Corporation (Conrail) and the Long Island Railroad (LIRR), over the decade 1976 to 1985, will exceed funds available from internal sources of private markets by $13 to $16 billion" (emphasis added).

The forecast $13 to $16 billion "shortfall," as it came to be known, proved to be a key issue in influencing the further deregulation of railroads under the Staggers Rail Act of 1980 (Staggers Act). The projected failure of the railroads to earn sufficient revenues and the implied threat of the necessity for federal bailout was used by railroad industry supporters in their successful effort to pass the Staggers Act. The Congressional Record of the passage of the Staggers Act contains numerous references to the forecast shortfall and other conclusions of the DOT report. The Staggers Act itself, in its findings (Sec. 2(7)), stated that:

> by 1985, there will be a capital shortfail within the railroad industry of between $16,000,000,000 and $20,000,000,000.

The perception of a "shortfall" still exists and the railroad industry continues to use it in support of the argument that their industry remains in dire financial need. Although some supporters acknowledge that the original $13-$16 billion shortfall forecast may not have fully materialized, they still believe some shortfall exits. No one, however, has attempted to document what the financial performance of the railroad industry actually has been. This paper makes that much needed comparative analysis of the financial performance of the railroad operating companies. The financial performance of the railroad holding companies is not included in our analysis.

Using actual historical financial data for the period 1976-84 and making conservative estimates about 1985 performance,a comparative analysis of the total railroad industry shows that a significant capital surplus (defined as the difference between internally generated funds [1/] and capital expenditures) rather than a shortfall will occur over the 1976-85 period.

FINDINGS

Over the 1976-85 period:

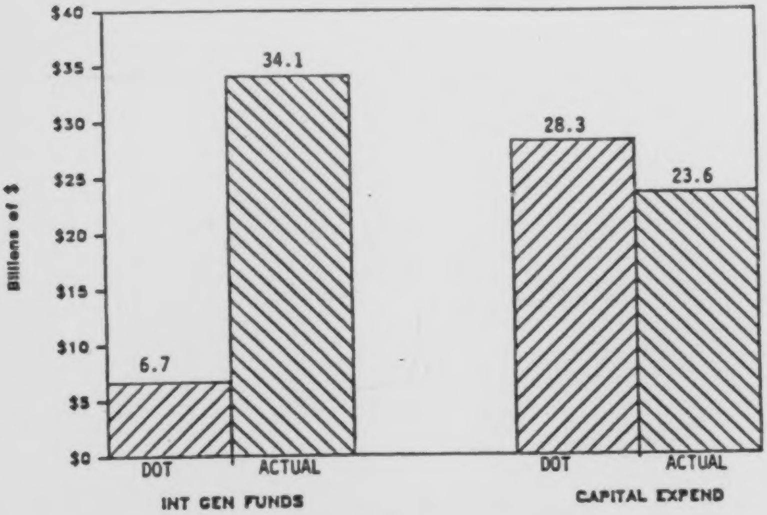
1. The railroad industry as a whole will experience a $10.5 billion surplus of internally generated funds over capital expenditures in contrast to DOT's forecast of a $21.6 billion shortfall.

2. Railroad industry actual internally generated funds will amount to $34.1 billion as opposed to DOT's forecast of $6.7 billion.

[1/] Internally generated funds represent the financial resources available to the corporation (from operations) to fund business activities. They include net income, depreciation charges and deferred taxes.

3. Railroad industry actual capital expenditures will amount to $23.6 billion as opposed to DOT's forecast of $28.3 billion.

TOTAL RAILROAD INDUSTRY INTERNALLY GENERATED FUNDS
AND
CAPITAL EXPENDITURES
1976-85
--DOT VS. ACTUAL--

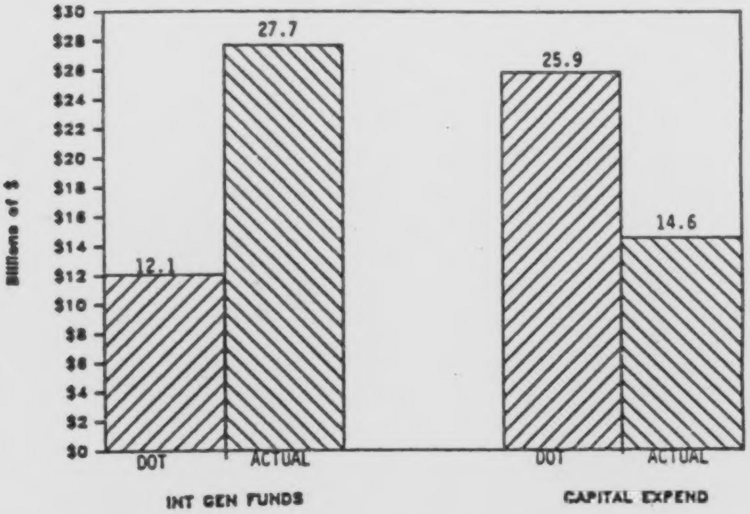


Note: The $21.6 billion DOT shortfall is the difference between $6.7 billion in internally generated funds and $28.3 billion in capital expenditures.

The $10.5 billion actual surplus is the difference between $34.1 billion in internally generated funds and $23.6 billion in capital expenditures.

4. Major railroad systems will show a $13.1 billion actual surplus of internally generated funds over capital expenditures in contrast to DOT's forecast of a $13.8 billion shortfall.

MAJOR RAILROAD SYSTEMS
INTERNALLY GENERATED FUNDS
AND
CAPITAL EXPENDITURES
1976-85
--DOT VS ACTUAL--



Note: The $13.8 billion DOT shortfall is the difference between $12.1 billion in internally generated funds and $25.9 billion in capital expenditures.

The $13.1 billion actual surplus is the difference between $27.7 billion in internally generated funds and $14.6 billion in capital expenditures.

5. Railroad industry actual net income will be a positive $17.9 billion as opposed to DOT's negative $5.7 billion forecast.

6. Major railroad systems actual net income will be $16.8 billion as opposed to DOT's forecast of approximately $1 billion.

COMPARISON OF ACTUAL AND DOT FORECAST
OF INTERNALLY GENERATED FUNDS
1976-85

(IN BILLIONS)

Total Railroad Industry	Actual	DOT
• Net Income	$17.9	($5.7)
• Depreciation	11.5	10.9
• Deferred Taxes & Other	4.7	1.5
Internally Generated Funds	$34.1	$6.7
Major Railroad Systems 1/		
• Net Income	$16.8	$ .9
• Depreciation	6.7	9.9
• Deferred Taxes & Other	4.2	1.3
Internally Generated Funds	$27.7	$12.1
Marginal Railroad Systems		
• Net Income	$1.1	($6.6)
• Depreciation	4.8	1.0
• Deferred Taxes & Other	.6	.3
Internally Generated Funds	$6.5	($5.3)

1/ CSX Corporation, Burlington Nortnern Railroad Company, Norfolk Southern Corporation, and Union Pacific Corporation

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Washington, DC 20036
July, 1985

RAILROAD CAPITAL SHORTFALL--OR SURPLUS?

INTRODUCTION

In October, 1978, the U.S. Department of Transportation (DOT) submitted a report to Congress entitled "A Prospective for Change in the Freight Railroad Industry." The report was prepared in response to the requirements of sections 504 and 901 of the Railroad Revitalization and Regulatory Reform Act of 1976 (the 4R Act). The primary purpose of the DOT report was to assess the capital needs of the railroad industry for the period 1976-1985 and determine whether those needs could be met by private sources of capital. In the event the capital requirements could not be met by private sources, an estimate of the financial assistance the federal government should provide was to be made.

The report concluded that: "requirements for funds by Class I railroads exclusive of Consolidated Rail Corporation (Conrail) and the Long Island Railroad (LIRR), over the decade 1976 to 1985, will exceed funds available from internal sources or private markets by $13 to $16 billion" (emphasis added).

The forecast requirement for funds or "shortfall", as it came to be known, was widely publicized by railroad industry supporters, who still continue to use it in support of their claim that the industry remains in dire financial need. Although some railroad supporters acknowledge that the original $13 - $16 billion shortfall forecast may not have fully materialized, they still believe some shortfall exists. They have not, however, attempted to document what the actual performance of the railroad industry has been with regard to generation of funds and capital expenditures.

Actual financial data reported by the railroads to the Interstate Commerce Commission for the period 1976-84, together with conservative estimates about 1985 performance, show that for the total railroad industry, a significant capital surplus (defined as the difference between internally generated funds and capital expenditures) will occur over the 1976-85 period rather than a shortfall.

SUMMARY OF FINDINGS

Over the 1976-85 period:

- The railroad industry as a whole will experience a $10.5 billion surplus of internally generated funds over capital expenditures in contrast to DOT's forecast of a $16.3 billion capital shortfall.
- Railroad industry actual internally generated funds will amount to $34.1 billion as opposed to DOT's forecast of $6.7 billion.
- Railroad industry actual capital expenditures will amount to $23.6 billion as opposed to DOT's forecast of $28.3 billion.
- Railroad industry actual net income will be a positive $17.9 billion as opposed to DOT's negative $5.7 billion forecast.
- Major railroad systems[1] will show a $13.1 billion surplus of internally generated funds over capital expenditures in contrast to DOT's forecast of a $13.8 billion capital shortfall.
- Major railroad systems actual net income will be $16.8 billion as opposed to DOT's forecast of approximately $1 billion.

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[1] CSX Corporation, Burlington Northern Railroad Company, Norfolk Southern Corporation, and Union Pacific Corporation. The systems are not only the major rail systems but also account for over 75 percent of all U.S. rail coal. Therefore, the terms major system and major coal-hauling system are used interchangeably.

DISCUSSION

Two major areas are addressed in this analysis: (1) The contrast between DOT's forecast of the railroad industry's internally generated funds and capital expenditures over the 1976-85 period and actual developments; and (2) the underlying reasons for the differences between DOT's forecast and actual results.

The analysis examined income statements, cash flow from operations and capital expenditures as reported by railroads to the ICC. Since the outstanding value of new debt issues and repayments remained essentially constant throughout the 1976-83 period (see Table 1, Appendix) we did not address them any further. The constant level of debt indicates that the railroad industry was able to finance most of its capital requirements through internally generated funds during the 1976-83 period. The comparative analysis, therefore, is limited to measuring the difference between internally generated funds and capital expenditures. A discussion of the analysis methodology is contained in the Appendix.

1. Difference Between Forecast and Actual Internally Generated Funds and Capital Expenditures

DOT forecast that the U.S. railroad industry would experience a cumulative capital shortfall of $16.3 billion over the 1976-85 period. A tabulation of the DOT statistics used to formulate this estimate is presented below.

DOT ESTIMATE OF THE RAILROAD INDUSTRY
CUMULATIVE CAPITAL SHORTFALL
1976-85

(IN BILLIONS)

Sources of Funds	
• Internally Generated Funds	$ 6.7
• Debt Proceeds	18.4
• Other	.9
Total	$26.0
Uses of Funds	
• Capital Expenditures	$28.3
• Debt Repayment	10.8
• Restoration of Working Capital	2.9
• Other	.3
Total	$42.3
CAPITAL SHORTFALL	($16.3)

The critical assumptions that drove the DOT forecast and resulted in the capital shortfall estimate were:

- A low level of internally generated funds;
- Heavy reliance on debt financing;
- A corresponding heavy debt repayment schedule; and,
- A relatively high rate of capital expenditures.

Internally generated funds represent the financial resources available to the corporation (from operations) to fund business activities. They include net income, depreciation charges and deferred taxes. Internally generated funds are a more useful measure of corporate financial health than net income alone. Changes in tax and depreciation laws over the study period have impacted reported net income. These changes in turn are reflected in depreciation and deferred charges. To account for the totality of these adjustments we expressed financial performance as the sum of net income, depreciation, and deferred taxes.

Actual railroad financial performance and the DOT forecast were contrasted for the following groups:

- The entire railroad industry (excluding Conrail);
- The major viable rail systems (i.e., the coal hauling railroads[2/]); and,
- The marginal rail systems.

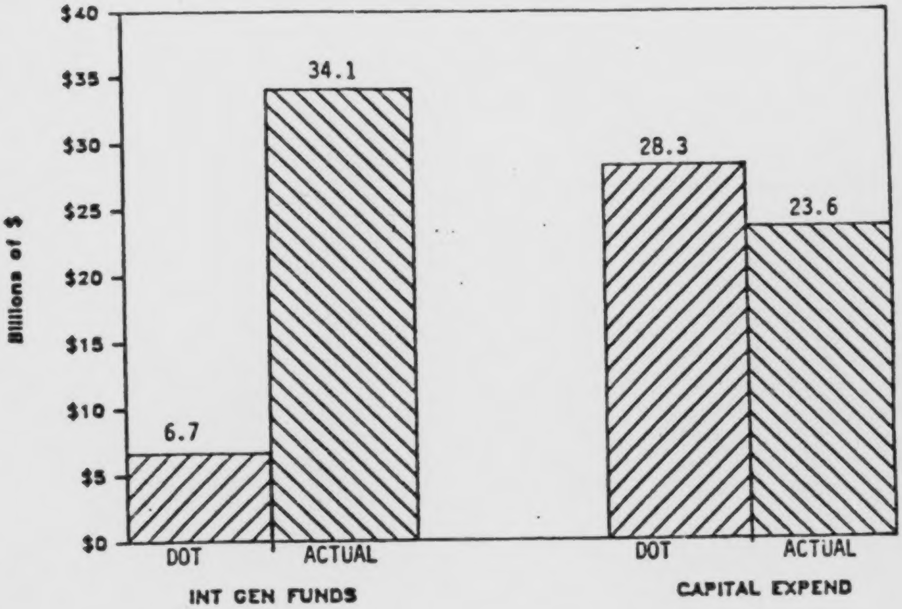
A detailed summary of this information is found in Table (2) and Figures 1-4 of the Appendix.

(a) Total Industry--DOT predicted that over the 1976-85 period, internally generated funds from operations for the entire industry would amount to **$6.7** billion. However, actual performance for the period resulted in internally generated funds that totaled **$34.1** billion. DOT also predicted total railroad industry capital expenditures of **$28.3** billion for the 1976-85 period. In comparison, actual capital expenditures have been **$23.6** billion.

The net result is that DOT forecast a significant capital shortfall between internally generated funds and capital expenditures during the 1976-85 period. In actuality, the railroad industry produced a **$10.5** billion capital surplus.

[2/] CSX Corporation, Burlington Northern Railroad Company, Norfolk Southern Corporation, and Union Pacific Corporation.

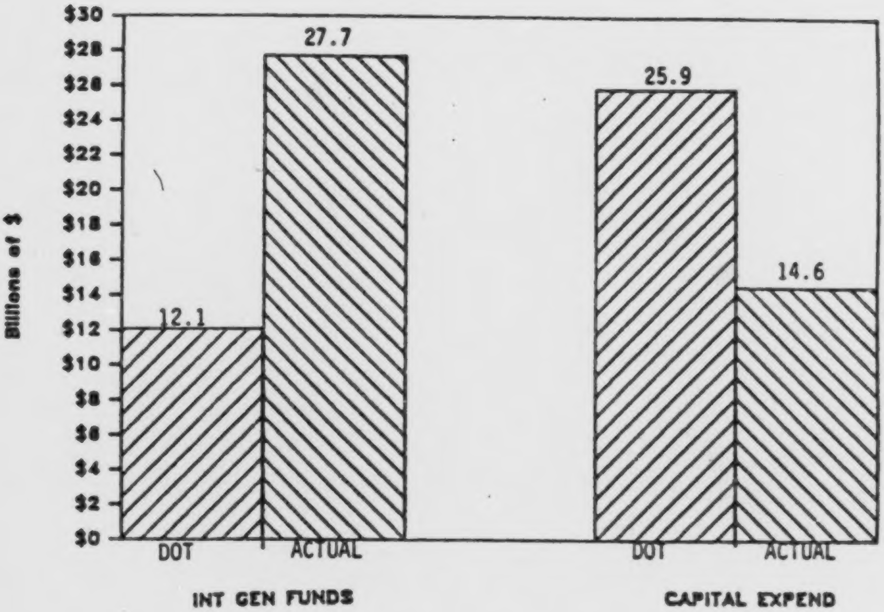
TOTAL RAILROAD INDUSTRY INTERNALLY GENERATED FUNDS
AND
CAPITAL EXPENDITURES
1976-85
--DOT VS. ACTUAL--



(b) Major Railroad Systems--For the major railroad systems, which carry most of the nation's coal, DOT predicted that internally generated funds for the period 1976-85 would total $12.1 billion, capital expenditures would amount to $25.9 billion and that a $13.8 billion capital shortfall would result.

The actual figures present a different picture. Over the 1976-85 period, the major railroad systems produced $27.7 billion in internally generated funds, capital expenditures totaled $14.6 billion and a $13.1 billion surplus existed between internally generated funds and capital expenditures.

MAJOR RAILROAD SYSTEMS
INTERNALLY GENERATED FUNDS
AND
CAPITAL EXPENDITURES
1976-85
--DOT VS ACTUAL--



(c) Marginal Railroad Systems[3]--In the case of marginal railroad systems, the actual internally generated funds from operations also exceeded DOT's forecast. For the 1976-85 period DOT predicted that marginal railroad systems would generate a negative $5.4 billion in funds from internal operations and would incur some $2.4 billion in capital expenditures. This resulted in a negative $7.8 billion difference between funds from operations and capital expenditures.

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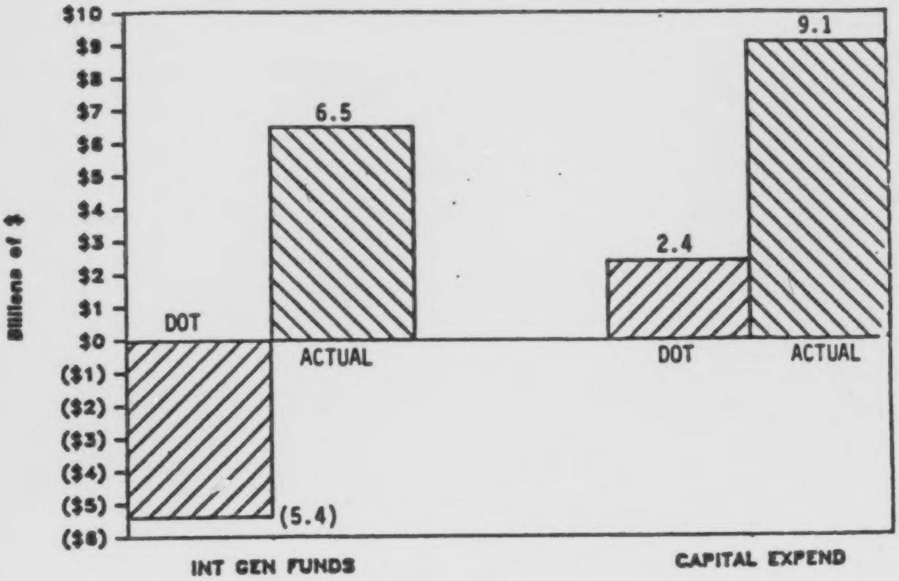
[3] Excluding Conrail and the Long Island Railroad.

Actual results present a different picture. Over the 1976-85 period, marginal railroad systems generated some $6.5 billion in funds from operations while capital expenditures totaled $9.1 billion. This yielded a difference between funds generated from internal operations and capital expenditures of a negative $2.6 billion for the 1976-85 period. This particular result in no way alters the prosperity of the major coal hauling railroads who benefited greatly from the 4R and Staggers Acts. Rather, it serves to highlight the fact that marginal railroads, without significant volumes of captive traffic (i.e., coal) have not been significantly helped by these legislative efforts.

MARGINAL RAILROAD SYSTEMS
INTERNALLY GENERATED FUNDS
AND CAPITAL EXPENDITURES
1976-85
--DOT VS. ACTUAL--



2. Reasons for Differences Between the DOT Forecast and Actual Results

The major differences between DOT's forecast and actual results center on the components of internally generated funds and capital expenditures. In the case of internally generated funds, the most obvious discrepancy exists in the area of net income. With capital expenditures, differences also exist, and these may be attributed to alternative assessments of traffic growth and the expenditures required to handle anticipated increased movements over the 1976-85 period.

(a) Net Income--DOT underestimated railroad industry ability to generate net income for the 1976-85 period. As can be seen in the following table, DOT predicted that the total railroad industry would experience a negative $5.7 billion in net income; the major rail systems would earn $.9 billion in net income; and, that the marginal rail systems would experience a net loss of $6.6 billion.

COMPARISON OF ACTUAL AND DOT FORECAST
OF INTERNALLY GENERATED FUNDS
1976-85

(IN BILLIONS)

Total Railroad Industry	Actual	DOT
• Net Income	$17.9	($5.7)
• Depreciation	11.5	10.9
• Deferred Taxes & Other	4.7	1.5
Internally Generated Funds	$34.1	$6.7
Major Railroad Systems		
• Net Income	$16.8	$ .9
• Depreciation	6.7	9.9
• Deferred Taxes & Other	4.2	1.3
Internally Generated Funds	$27.7	$12.1
Marginal Railroad Systems		
• Net Income	$1.1	($6.6)
• Depreciation	4.8	1.0
• Deferred Taxes & Other	.6	.3
Internally Generated Funds	$6.5	($5.3)

Source: See Methodology Discussion in Appendix.

The considerable margin of error in DOT's forecast is attributed to the unrealistic assumptions that were incorporated in their economic/financial model. DOT's model assumed that a high level of operating inefficiency would be maintained throughout the 1976-85 period. For example, DOT assumed a constant railroad operating ratio of 98.4 percent. Operating ratios are a generally accepted indicator of how well costs are being managed and contrasts operating expenses to railroad revenues. DOT's use of a constant operating ratio is particularly surprising in view of the fact that the actual industry average ratio for 1976 was already down to 96.5 percent. The ratio has subsequently improved to 87 percent for 1984.

Some of the major factors contributing to the improved operating ratio since 1976 are:

- Increased use of more efficient unit trains;
- Improvements in fuel efficiency of equipment;
- Increased worker productivity;
- More efficient use of equipment; and,
- Greater reliance on shipper owned railroad equipment and facilities.

To offset the predicted shortage in internally generated funds, the DOT model assumed that the railroad industry would incur additional amounts of debt to:

- Expand system capacity;
- Accelerate expenditures on deferred track maintenance; and,
- Pay appreciable dividends.

These unrealistic assumptions resulted in an income statement that forecast a $5.7 billion loss in net income over the 1976-85 period. It is unclear why DOT assumed that management and institutional lenders would have continued to invest increasing amounts of capital in an industry that paid declining if not negative financial returns over the 1976-85 period.

There is reason to believe that DOT's estimate was viewed by the railroad industry itself as an unlikely scenario when it was prepared. In accordance with Section 504(a) of the 4R Act, DOT solicited financial forecasts from the Class I railroads for use in preparation of its Report to Congress. A tabulation of individual railroad submissions indicated that the railroad industry expected to generate $23 billion in funds from operations during the 1976-85 period as opposed to DOT's prediction of $6.7 billion. Furthermore, the railroads indicated that they believed the industry would not experience a capital shortage over the 1976-85 period. DOT dismissed the railroad industry's submissions as overly optimistic and relied instead on its internal estimates and forecasts.

(b) Growth Projections--The DOT study assumed that economic growth would be maintained at a rate of 3.9 percent per year during the forecast period. DOT also projected continued significant traffic increases over the 1976-85 period. Based on these assumptions, cumulative railroad traffic revenues over the period were forecast to be $234 billion.

The DOT assumptions regarding economic and traffic growth were overly optimistic. An examination of statistics indicates that the volume of annual traffic transported by rail declined from 2.3 to 1.9 billion tons during the 1976-83 period. Actual revenues over the 1976-85 period, by comparison, were $219 billion. A detailed breakdown of actual and forecast revenues is shown in Table 3 of the Appendix. In spite of this lower than predicted cumulative revenue, the railroad industry demonstrated a sizeable capital surplus instead of the forecast shortfall.

EDISON ELECTRIC
INSTITUTE The association of electric companies
1111 19th Street, N.W.
Washington, DC 20036

JULY, 1985

APPENDIX

COMPARATIVE ANALYSIS METHODOLOGY

The original DOT study utilized extensive modeling of many variables to arrive at statistics for total sources and uses of capital. Because actual historical data was available for nine of the ten study years (1976-84), it was not necessary to repeat the modeling effort to perform a comparative analysis. For the remaining year of the study, 1985, preliminary results for 1984 were used.

The comparative analysis was performed in essentially the same manner as in the DOT study. The DOT study developed a railroad industry income statement, funds from operations estimate and source and use of funds projection. DOT's estimate of capital shortages was calculated by contrasting the difference between internal funds generation supplemented by debt financings and the anticipated use of funds.

Capital Sources

- Net Income After Taxes and Dividends
- Depreciation
- Debt Financing

less

Capital Use

- Capital Expenditures
- Debt Repayments
- Restoration of Deficiencies in Working Capital

equals

Capital Surplus (Shortfall)

The comparative analysis was restricted to actual income statements, funds from operations and capital expenditures as reported by the railroads to the ICC. Debt issues and debt repayments were not examined because AAR statistics indicate that railroad industry debt (long term and equipment obligations) remained essentially constant over the 1976-1983 period (see Table 1). This would indicate little, if any, increased reliance on debt for financing operations during the period.

The DOT methodology analyzed three industry groupings (all excluding Conrail):

- Total railroad industry;
- Major systems considered economically viable; and
- Marginal rail systems.

The comparative analysis considered the following groupings (also excluding Conrail):

- Total railroad industry;
- Major rail systems (BN, CSX, NS and UP); and
- Balance of the rail industry

For the sake of consistency, the analysis assumed that railroads which are currently part of the four coal hauling systems analyzed were so throughout the entire 1976-1985 period.

Distinguishing between the major coal hauling systems and the rest of the railroad industry highlights the fact that the major coal haulers have always been financially healthy and have enjoyed disproportionate gains under the Staggers Act.

FIGURE #1

INT. GEN. FUNDS & CAPITAL EXPEND. (DOT)

Total US Railroad Industry

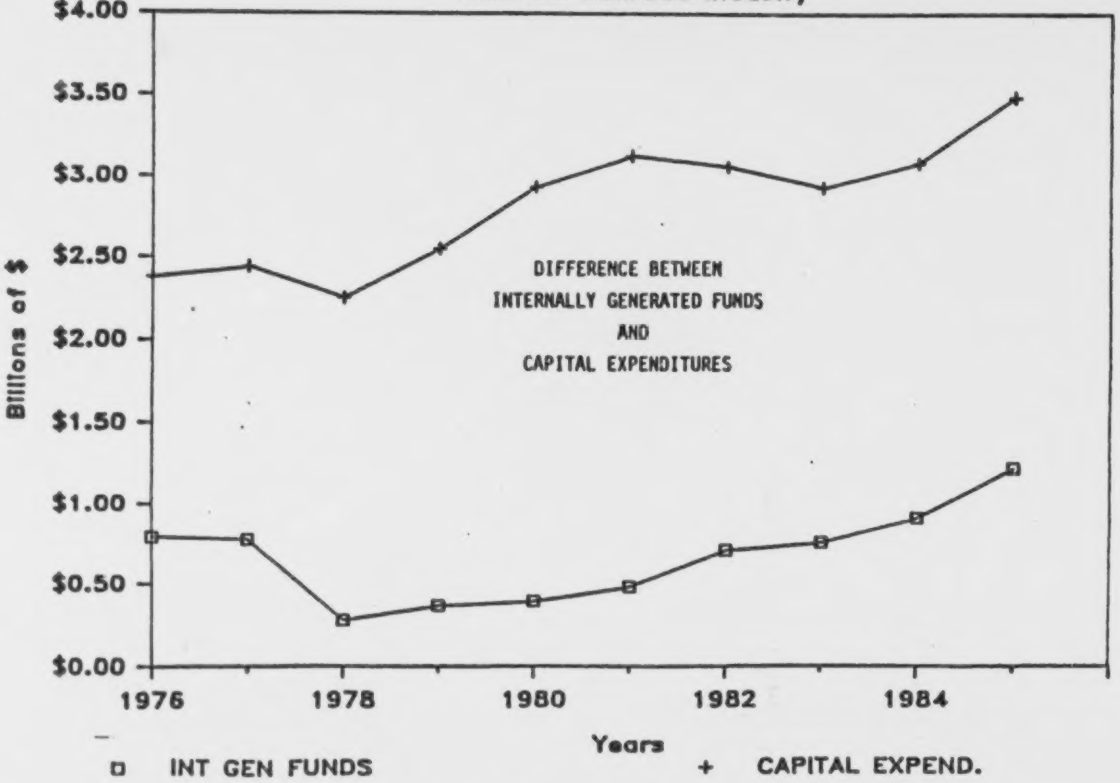


FIGURE #2

INT. GEN. FUNDS & CAP. EXPEND. (ACTUAL)

Total US Railroad Industry

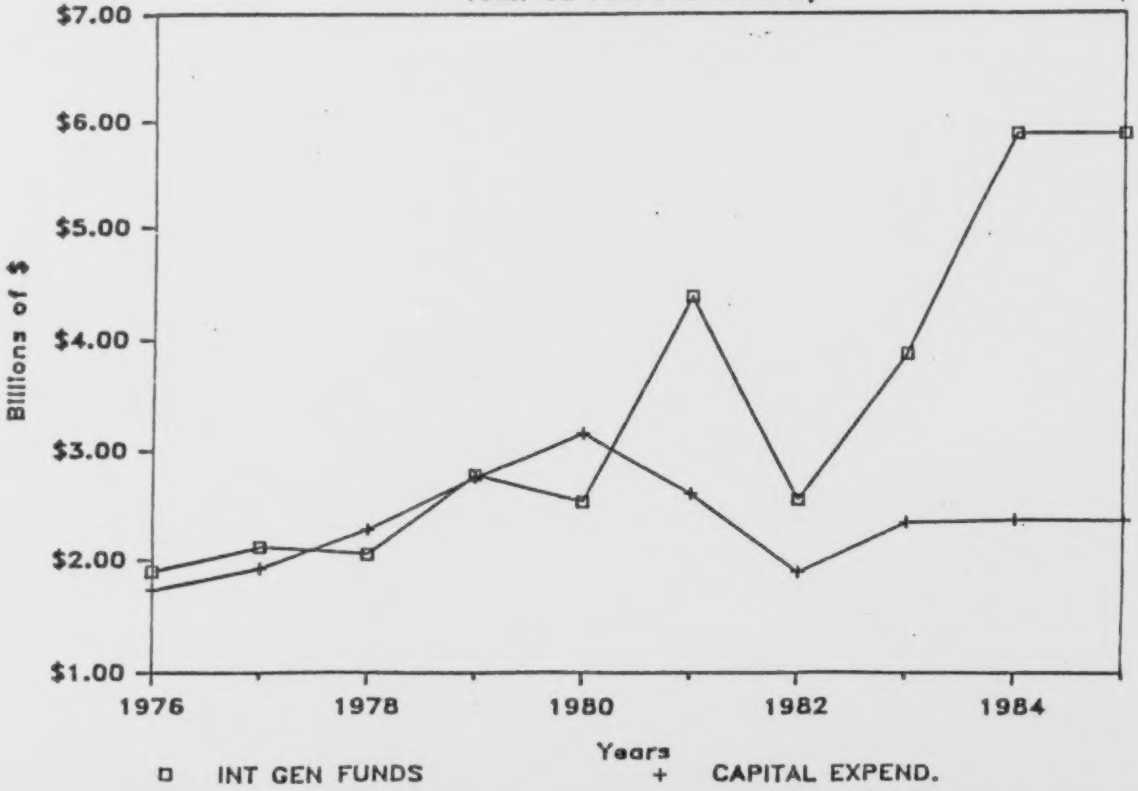


FIGURE #3

DOT & ACTUAL INTERNALLY GEN. FUNDS

Total US Railroad Industry

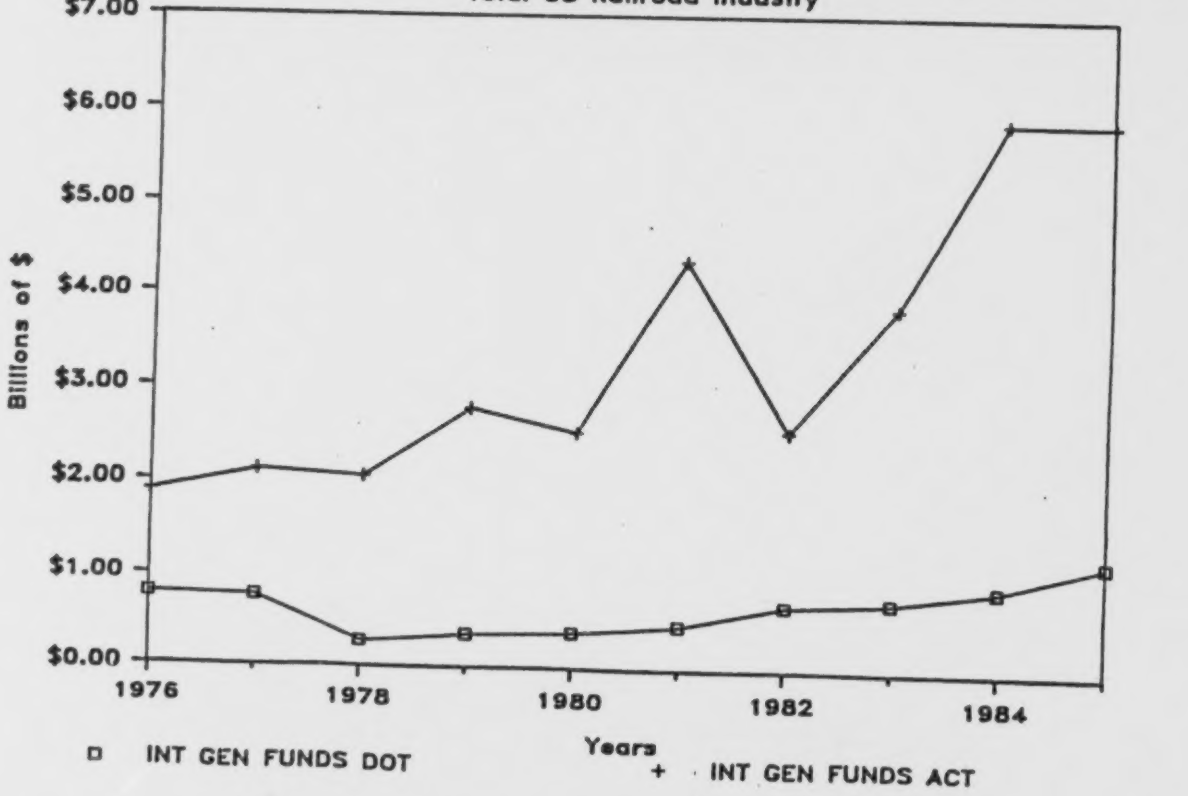


FIGURE #4

DOT AND ACTUAL CAPITAL EXPENDITURES

Total US Railroad Industry

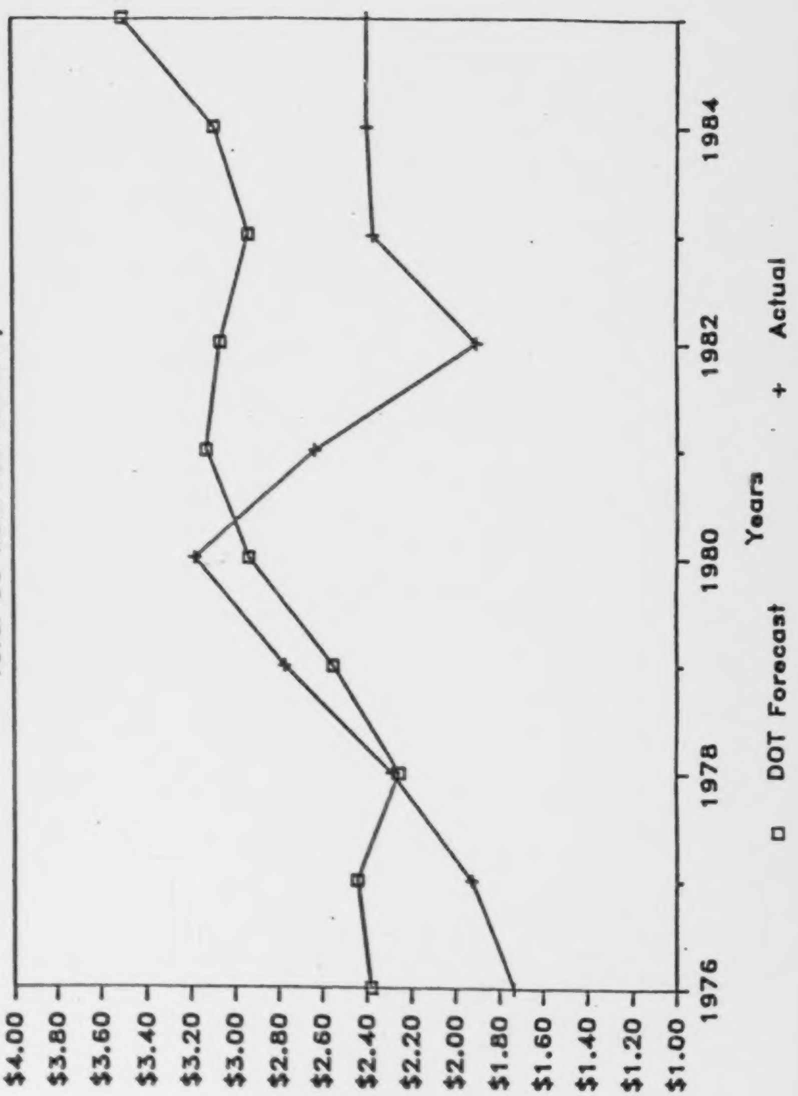


Table 1

ACTUAL RAILROAD LONG-TERM DEBT AND EQUIPMENT OBLIGATIONS

(MILLIONS OF DOLLARS)

Year	Long Term Debt Due After One Year	Equipment Obligations Outstanding End of Year	Total Debt
1975	$11,347	$5,179	$16,526
1976	10,268	5,363	15,631
1977	11,168	5,674	16,842
1978	11,413	5,732	17,145
1979	11,646	6,116	17,762
1980	12,626	6,694	19,320
1981	12,376	6,143	18,519
1982	11,712	5,741	17,453
1983	11,069	5,131	16,200

Source: Railroad Ten-Year Trends--1984 Edition, Association of American Railroads

Table 2

COMPARISON OF ACTUAL AND DOT FORECAST INTERNALLY GENERATED FUNDS AND CAPITAL EXPENDITURES 1976-85

(IN BILLIONS)

TOTAL RAILROAD INDUSTRY	ACTUAL 1/	DOT 2/
• Internally Generated Funds*	$34.1	$ 6.7
• Capital Expenditures	23.6	28.3
Difference	$10.5	$(21.6)
MAJOR RAILROAD SYSTEMS		
• Internally Generated Funds*	$27.7	$ 12.1
• Capital Expenditures	14.6	25.9
Difference	$13.1	$(13.8)
MARGINAL RAILROAD SYSTEMS		
• Internally Generated Funds*	$ 6.5	$(5.4)
• Capital Expenditures	9.1	2.4
Difference	$(2.6)	$(7.8)

* Net income after dividends, depreciation and deferred taxes.

Source: 1/ Interstate Commerce Commission Transport Statistics; and, Railroad Annual Reports to the ICC.
2/ DOT Study.

Table 3

COMPARISON OF ACTUAL AND DOT FORECAST TOTAL RAILROAD INCOME STATEMENT 1976-85

(IN BILLIONS)

	ACTUAL 1/	DOT 2/
• Total Revenues	$218.8	$234.2
• Operating Expenditures	(202.3)	(230.4)
• Net Operating Income	16.5	3.8
• Other Income	11.7	7.3
• Income Available for Fixed Charges	28.2	11.1
• Fixed Charges	(8.2)	(9.4)
• Net Ordinary Income	20.2	1.7
• Income Taxes	(5.5)	(3.0)
• Net Income Before Dividends	14.5	(1.3)

Source: 1/ Interstate Commerce Commission Transport Statistics; and, Railroad Annual Reports to the ICC.
2/ DOT Study.

Senator **Grassley**. OK. Go ahead, Mr. Purcell.

STATEMENT OF KEN PURCELL

Mr. **Purcell**. Thank you, Senator. Thank you for scheduling this hearing and for allowing us an opportunity to testify before you. I, too, will summarize my statement, the complete text of which I ask to be submitted into the record.

My name is Ken Purcell, and I'm here representing my company, Iowa-Illinois Gas and Electric Co., in Davenport, IA, and the more than 175,000 electric customers we serve.

Last year, Iowa-Illinois generated 59 percent of its electric energy from coal-fired plants. All of the coal that those plants received was shipped exclusively by rail, and all of it came from mines served by a single railroad.

This brief description of the relationship between our company and the railroad industry makes it clear that our company and our customers need this Nation's railroads, are dependent on them, and are more vulnerable than most to potential abuses in rail transport charges.

When it passed the Staggers Rail Act in 1980, the U.S. Congress made clear its intention to bolster the economic health of America's railroad industry by injecting a healthy dose of competition. Iowa-Illinois does not quarrel with either this end or the means chosen to reach it. Indeed, a strong railroad industry is essential to the well-being of the electrical utility industry.

The problem that Iowa-Illinois has with the Staggers Act is the failure of the Interstate Commerce Commission to achieve another avowed goal of Congress: to guarantee fair and reasonable rates for so-called "captive shippers," whose commodities travel routes where no viable transportation alternative exists.

Iowa-Illinois counts a full 90 percent of the slightly more than 1 million tons of coal it purchased in 1984 in this captive shipper category. The company's largest plant, the Louisa Generating Station in southeastern Iowa, is a captive plant. The 930,000 tons of coal the company purchased to fuel the plant last year was mined in Wyoming's Powder River Basin and shipped by the Burlington Northern and Milwaukee Road railroads; no other viable means of transportation existed. Since the plant started receiving coal in 1982, comparisons of current rates with those in effect before Staggers was passed, are impossible. But even in the two years of the plant's operation, a clear trend is discernible. From 1982, to 1984, the price of coal at the Powder River Basin's Sunedco mine decreased by 35 percent. The cost of transporting that coal, however, increased by 12 percent during the same period.

A pre-Staggers comparison is possible for our company's Riverside generating station near the Quad Cities, and the changes there are striking. From 1980, the first year of a coal delivery contract with the Buckhart mine in southern Illinois, and also the year that Staggers was passed, until 1984, the price of coal burned at Riverside rose 23 percent, while the Burlington Northern's tariff rate for delivering that coal rose by 50 percent.

Iowa-Illinois feels that S. 447, the DeConcini bill before this subcommittee this afternoon, is a well-intentioned bill that, if it were passed into law, would create the potential for resolving some of the problems that the captive rail shipper faces. However, the approach that S. 447 takes—that of amending the Sherman Antitrust Act—seems to us to be a roundabout way of dealing with these problems, and could unintentionally create more of a hindrance than a help in resolving them.

In offering antitrust proceedings and injuctive relief through the Federal court system as the captive shipper's means of relief, S. 447 relies on one of the most cumbersome and time-consuming areas of statutory law. Decisions in antitrust procedings commonly come several years after they are first filed. While such delays are frustrating to any petitioner, in the case of proceedings brought by an electric utility, such a time lapse would virtually prohibit us from returning to the customers who actually paid the rates any refunds that might be ordered from an antitrust action.

Furthermore, Federal courts presented the task of ruling on alleged anticompetitive practices by railroads would be likely to use as precedents the rulings of other courts upholding the actions of the Interstate Commerce Commission in this area. Such precedents would further reduce the effectiveness of the relief offered by S. 447, since the ICC rulings and the unwillingness of Federal courts to overturn them are precisely the problems that the captive shipper faces today.

Iowa-Illinois feels that a better approach would be to amend the Staggers Rail Act directly by mandating adherence by the ICC to some of that law's most basic provisions. This is the approach used in two bills currently pending before the House Energy and Commerce and the Senate Commerce Committees. These bills, called the Consumer Rail Equity Act, are numbered S. 477 in the Senate and H.R. 1190 in the House. Unlike S. 447, they rely on legislative directives aimed at a specific administrative agency, rather than the judicial system as a whole. Iowa-Illinios feels that such an approach would guarantee more specific and more timely response than would adopting language aimed at affecting judicial interpretation.

Thank you, again, for scheduling this hearing, and I'd be happy to answer any questions.

[Prepared statement follows:]

COMMENTS OF
IOWA-ILLINOIS GAS AND ELECTRIC COMPANY

Introduction

Senator Grassley, thank you for the opportunity to appear before your subcommittee this afternoon.

My name is Ken Purcell. I am here representing Iowa-Illinois Gas and Electric Company and the more than 175,000 electric customers we serve.

The subject of this hearing is one that effects the electric utility industry more than almost any other sector of our economy. Coal is the fuel used to produce over 53 percent of the nation's electricity each year. The overwhelming majority of that coal is shipped by rail. More importantly, a full 85 percent of the coal burned by electric utilities comes from mines served by a single railroad.

Last year, Iowa-Illinois generated 59 percent of its electric energy from coal-fired plants. All of the coal those plants received was shipped exclusively by rail, and all of it came from mines served by a single railroad.

These few facts about the relationship between our industry and the railroad industry make it clear that America's electric utilities and their customers need this nation's railroads, are dependent on them--and are more vulnerable than most to potential abuses in rail transport charges.

When it passed the Staggers Rail Act in 1980, the U. S. Congress made clear its intention to bolster the economic health of America's railroad industry by injecting a healthy dose of competition. Iowa-Illinois does not quarrel with either this end or the means chosen to reach it. Indeed, a strong railroad industry is essential to the well-being of the electric utility industry.

The problem that Iowa-Illinois has with the Staggers Act is the failure of the Interstate Commerce Commission (ICC) and, to a lesser extent, the language of the statute itself, to achieve another avowed goal of Congress: to guarantee fair and reasonable rates for so-called "captive shippers" whose commodities travel routes where no viable transportation alternative exists.

Iowa-Illinois counts 90 percent of the slightly more than one million tons of coal it purchased in 1984 in this captive shipper category. The Company's largest plant, the Louisa Generating Station in southeastern Iowa, is a captive plant. The 930,000 tons of coal the Company purchased to fuel the plant in 1984 was mined in Wyoming's Powder River Basin and shipped by the Burlington Northern and Milwaukee Road railroads; no other viable means of transportation existed. Since the plant started receiving coal in 1982, comparisons of current rates with those in effect before Staggers was passed are impossible. But even in the two years of the plant's operation, a clear trend is discernible. From 1982 to 1984, the price of coal at the Powder River Basin's Sunedco mine decreased by 35%. The cost of transporting that coal, however, increased by 12% during the same period.

A pre-Staggers comparison is possible for our Company's Riverside Generating Station near the Quad-Cities, however, and the changes are striking. From 1980, the first year of a coal delivery contract with the Buckhart mine in southern Illinois and also the year that Staggers was passed, until 1984, the price of the coal burned at Riverside rose 23 percent while the Burlington Northern's tariff rate for delivering that coal rose by 50 percent.

Iowa-Illinois also has substantial ownership shares in three coal-burning generating units--the Ottumwa Unit 1 in Chillicothe, Iowa, the Neal 3 unit near Sioux City, and Council Bluffs Unit 3--that are captive to one railroad's transportation system. The Company's positions on S. 447 and proposed legislation to amend the Staggers Rail Act apply as much or more to those plants, from which we receive

44 percent of our energy, than to the eastern Iowa plants that the Company operates.

Before describing Iowa-Illinois' position on S. 447 and proposed changes to the Staggers Rail Act, I would emphasize three key points about our position. First, Iowa-Illinois does not seek repeal of Staggers or an end to any of the benefits that the law has brought to the U. S. economy. Second, Iowa-Illinois does not seek a return to the burdensome regulation that plagued the railroad industry prior to Staggers. Finally, Iowa-Illinois does seek changes that would increase the protection of captive shippers, especially shippers of coal but also shippers of other bulk commodities and manufactured goods.

Iowa-Illinois feels that S. 447, the Rail Anti-Monopoly Act of 1985, is a well-intentioned bill that, if passed into law, would create the potential for resolving some of the problems faced by the captive rail shipper. However, the approach that S. 447 takes, that of amending the Sherman Anti-Trust Act, seems to be a roundabout way of dealing with these problems, and could unintentionally create more of a hindrance than a help in resolving them.

In offering anti-trust proceedings and injunctive relief through the federal court system as the captive shipper's means of relief, S. 447 relies on one of the most cumbersome and time-consuming areas of statutory law. Decisions in anti-trust proceedings commonly come several years after they are first filed. While such delays are frustrating to any petitioner, in the case of proceedings brought by an electric utility such a time lapse would virtually prohibit a company from returning to the customers who actually paid them any refunds of unreasonable transport rates gained through the courts.

Furthermore, federal courts presented the task of ruling on alleged anti-competitive practices by railroads would be likely to use as precedents the rulings of other courts upholding the actions of the Interstate Commerce Commission in this area. Such precedents would further reduce the effectiveness of the relief offered by S. 447, since the ICC rulings and the unwillingness of federal courts to overturn them are precisely the problems that the captive shipper faces today.

Iowa-Illinois feels that a better approach would be to amend the Staggers Rail Act directly by mandating adherence by the ICC to some of that law's most basic principles. This is the approach used in two bills currently pending before the Energy committees of both houses of Congress. These bills, called the Consumer Rail Equity Act, are numbered S. 477 and H.R. 1190, respectively. Unlike S. 447, they rely on legislative directives aimed at a specific administrative agency rather than the judicial system as a whole. Iowa-Illinois feels that such an approach would guarantee more specific and more timely response than would adopting language aimed at affecting judicial interpretation.

In using this approach, the Consumer Rail Equity Act deals specifically with several important issues--including reciprocal switching, joint rates, and line abandonments--that S. 447 does not. A brief description of just one of these issues shows why Iowa-Illinois strongly supports the Consumer Rail Equity Act and has urged Iowa's congressional delegation to work for its passage.

Under current law, even if the ICC finds that a captive shipper is being charged an unreasonable transport rate, the agency cannot order a railroad to reduce that rate unless it finds that the railroad is revenue adequate. Under the standard for this revenue adequacy test currently being used by the ICC, that agency has never, in the five years since Staggers was enacted, found a railroad to be revenue adequate. These findings have produced anomalies like that of Norfolk Southern, which recently purchased North American Van Lines for $315 million and has made a much-publicized offer of $1.2 billion for CONRAIL, being found to be revenue inadequate by the ICC.

To end these ludicrous findings, the Consumer Rail Equity Act would require the ICC, in determining revenue adequacy, to consider several market-based indicators of a railroad's financial health, and to determine the value of a railroad's assets on a basis more consistent with the actual cost of providing transportation service.

In summary, then, Iowa-Illinois feels that S. 447 is a well-intentioned bill that could offer limited relief to this nation's captive rail shippers. However, we feel strongly that the Consumer Rail Equity Act presents the best means of protecting captive shippers while maintaining the benefits that have accrued to the railroad industry since the passage of the Staggers Rail Act. We urge this subcommittee and you personally, Senator, to do everything you can to see that the provisions of this latter bill become law.

Thank you again for this chance to testify before your subcommittee.

Senator **Grassley**. OK. Jerry.

STATEMENT OF JERRY D. PARKIN

Mr. **Parkin**. Thank you, Sentor Grassley. Again, I reiterate our thanks for allowing us to testify here today.

I represent Iowa Power & Light Co. of Des Moines, IA, which is the electrical utility subsidiary of Iowa Resources, Inc. Iowa Power is involved in the generation, transmission and distribution of electricity to over 232,000 customers in central and southwest Iowa. The major powerplant we operate is Council Bluffs power station, unit No. 3, which went on line in the late 1970's. It is a 650-megawatt unit which exclusively burns coal from the Powder River basin in Gillette, WY.

In our view, S. 447, which seeks to place the rail industry within the scope of the antitrust laws, does not really address the problems faced by the electric utilities as captive shippers. It is our feeling that the true problem rests with the Interstate Commerce Commission and its interpretation of the Staggers Rail Act, which was enacted by Congress in 1980.

The Staggers Rail Act provides the framework for a useful mechanism to enhance the railroad industry, while at the same time protecting the interest of the shippers. The implementation of the act by the Interstate Commerce Commission, however, has been in the interest of the railroads, and not in the interest of the shippers.

I've made some specific points in my testimony as to how we might be able to improve the Staggers Act. I don't want to take the time going through those today. We don't feel that wholesale revision of Staggers is necessary, but we do feel that there needs to be some fine tuning which would, in fact, give the ICC some more direction as to which way they should go in their interpretation of the law.

Obviously, our comments today do not address all of our concerns, and they merely are there to indicate that we believe some of the problems are there and need to be addressed. We are not in favor of the reregualtion of the Nation's rail industry, nor do we support the wholesale revision of current laws. Our major concern is that we are treated fairly and that we and our customers do not bear a disproportionate burden of the rail cost.

Electric utilities are vitally interested in the financial health of the railroad industry, yet we strongly believe that we must be able to protect ourselves, as companies, and our customers, who ultimately bear the costs of rail transportation. Coal is still the prevalent generation fuel in Iowa, and will remain that way for years to come. The only way for us to get this coal to our plants is by rail. Our customers demand that we do all we can to eliminate arbitrarily inflated coal transportation costs, and we do hope that we can continue to do that.

We've been in a situation where our company has been in court with the Burlington Northern for several years now over a disagreement on coal rates from the Powder River Basin to our Council Bluffs station, and this has, to us, gone on and on, and several million dollars are at stake right now of our customers' money.

With that, I'll let you ask any questions you want. Thank you.

[Prepared statement follows:]

STATEMENT OF
JERRY D. PARKIN
MANAGER OF GOVERNMENT AFFAIRS
IOWA POWER AND LIGHT COMPANY
DES MOINES, IOWA

My name is Jerry Parkin, and I am Manager of Government Affairs for Iowa Power and Light Company, the electric utility subsidiary of Iowa Resources Inc., which is headquartered in Des Moines, Iowa. Iowa Power is involved in the generation, transmission and distribution of electricity to over 232,000 residential, commercial and industrial customers in Central and Southwest Iowa.

Senator Grassley, we appreciate your holding this hearing, thereby providing us the opportunity to submit this statement for the record.

In our view, S. 447, which seeks to place the rail industry within the scope of the anti-trust laws, does not really address the problem faced by electric utilities as captive shippers. It is our feeling that the true problem rests with the Interstate Commerce Commission and its interpretation of the Staggers Rail Act, which was enacted by Congress in 1980.

The Staggers Rail Act provides the framework for a useful mechanism to enhance the railroad industry while at the same time, protecting the interests of the shippers. The implementation of this act by the Interstate Commerce Commission, however, has been in the interest of the railroads and not in the interests of the shippers.

The ICC apparently has made the assumption that shippers will all benefit from financially sound rail systems. This is true only if those same shippers can afford the use of the system. The determination of financial soundness, referred to as "revenue adequacy" in the Staggers Act, is based upon arbitrary definitions contained in the act. The protection for shippers was to come under the Cost Accounting Review Board, which was finally established in 1985, five years after adoption of the Staggers Act.

The ICC has not adequately addressed the problems that occur for captive shippers, and therefore we recommend that the Staggers Act be reopened and amended. In particular, we would recommend that the following be considered:

1) The test for market dominance be changed so that if a shipper is served by a single railroad, market dominance will be presumed unless the railroad can show that effective competition from other carriers or modes of transportation exists for the shipment in question.

2) Revenue adequacy be determined by requiring the ICC to consider several economic indicators of the railroad's financial health. Further, if the ICC should find that a railroad must charge differential rates to achieve or maintain "revenue adequacy," it must also determine that the railroad has fairly allocated among all of its captive shippers the burden of producing revenues necessary to achieve or maintain revenue adequacy.

3) Finally, the Act should be amended to adequately address the issue of reciprocal switching. The ICC should be able to order reciprocal switching agreements where such agreements are necessary to provide competitive rail service. Reciprocal switching can enhance competition, provide an avenue to eliminate barriers for captive shippers, avoid duplication of rail lines thereby avoiding the unnecessary use of capital, and still enhance the market for the carriers themselves.

Obviously this brief statement does not address all of our concerns, but is merely intended to indicate where we believe some of the major problems to be. We are not in favor of the re-regulation of the nation's rail industry, nor do we support the wholesale revision of the current law. We are concerned that we be treated fairly and that we and our customers do not bear a disproportionate burden of rail costs.

Electric utilities are vitally interested in the financial health of the railroad industry, yet we strongly believe that we must protect ourselves as companies, and our customers, who ultimately bear the costs of rail transportation. Coal is still the prevalent generation fuel in Iowa, and the only way for us to get this coal to our plants is by rail. Our customers demand that we do all that we can to eliminate arbitrarily inflated coal transportation costs.

Thank you

Senator **Grassley**. Let me start out with an accusation that's been made by some, that certain utilities are less than enthusiastic about S. 447 because it may be applicable not only to the rail industry, but also to the utility companies, and your companies would be required to let others have access to transportation lines at a reasonable rate, using the present legal language. Do any of you fear that about S. 447? And if so, does that have anything to do with more support for S. 477 than S. 447?

Let me suggest, too, that even though I look at one person, the idea is that if any of you want to respond in addition to what the one person said, that's all right.

Mr. **Pitner**. First of all, Senator, with regard to the capacity that's available in comparing the utility list of the railroad industry, you must bear in mind that you're not comparing apples to apples. Utilities invest money because they are obligated to serve, and that as long as yes, there is indeed fair compensation for the use of that excess capacity, if there is any excess capacity, then I don't think the utilities are going to be all that mindful. So we do not have the choice of building a line or not. When customers demand service, we build, and our obligation to serve requires a certain return, and to have that return eroded and your service territory eroded, without the right to not build or build, puts us a little bit in jeopardy that the railroads might not suffer.

Second, FERC right now has got a notice-of-inquiry procedure before it regarding utility transactions and transmissions. And I think, in due time, the position of the industry will be very apparent, but so far, from reading the comments that I have, the major concern is the technical complications from utility transmission lines and allotting it to free wheeling. And again, to get back to fair cost and access to that, and that requires fair competition for the technical requisite that it takes with regard to electricity and reliability of service, but I don't believe the railroad industry would ultimately suffer from the access.

But really, we're not looking to equal access. We think that the problem can be solved through the Staggers Act. While your question is fair, I don't think the utility industry is on record of not welcoming equal access to transmission. I think they have a lot of concerns, and I think the notice of inquiry before FERC is being discussed today.

Senator **GRASSLEY**. Is there any further comment from the other three of you? OK. I would direct a question to Mr. Stoll, because you illustrated the problem in your testimony regarding the rate of return on investment on delivery of Neal-4 coal, and I think you did that at 93 percent, as opposed to an overall return rate of 16 percent. Do you know why this might be the case? And also, I'd like to have you comment on why there is a difference in contract price at $10.06 and $14.03 for the same mileage on the same railroad.

Mr. **STOLL**. Let me approach, first, the comment on the difference in the same mileage and the same railroad. They are not the same railroad, Senator. They are the same railroad from Omaha-Council Bluffs to the Neal station, about 90 miles. That's the CNW. Under the $10 tariff, the coal originates in the Hannah Basin, which is in south-central Wyoming. Under the $14 tariff, the coal originates on the BN out of the Powder River Basin. So the originating railroads are different. The mileage is almost identical. There is only about 20 miles difference between the two hauls.

Now, the $10 tariff was negotiated back in the late 1960's or early 1970's, when the UP Railroad was attempting to open up their coal reserves in south-central Wyoming, and they were competing against the possibility of us moving some coal out of either Oklahoma or Illinois, and that's when we got that rate established. We had a better agreement, and they have abided by that agreement.

The $14.03 no-charge rate is actually an escalated rate that was established by the ICC in our present proceeding, and that proceeding started in 1978. We tried to negotiate a rate with the BN and CNW and could not. They filed a rate with the ICC. We filed a complaint, and the ICC came down with this rate. It was appealed to the courts and remanded back to the ICC, and that's where it stands today.

To address the 93-percent rate of return indicated here, this from a study made by EEI, and these are the figures that were set out in that study, using what we call normal utility accounting principles to determine the rate of return on the investment. I think the details of that 93 percent are in a study that I left with my paper.

Senator **GRASSLEY**. Any further comment by either of the three of you? OK.

Now, some of you did mention in your testimony how much electricity from your specific company is produced by coal. But, for the record at this point, I'd also like to have, if you could estimate for me, how much your customers have overpaid as a result of the implicit misinterpretation by the ICC of the Staggers Act in regard to your being captive shippers and your customers paying for that. If you don't have the latter, I'd like to have that submitted in writing, assuming you have something along that line. But if you can tell me now, I'd appreciate it. I'm sure you can answer at least the first part.

Mr. **Parkin**. In the case of Iowa Power, during the normal year we would get between 50 and 60 percent of the electricity in our system from coal-fired generation. We have a 25-year contract with a nuclear station in Brownsville, NE, which provides somewhere between 40 and 50 percent of the power.

Regarding payment, I'd hesitate to give you an exact figure, although I seem to recall that over the life of the contract that we have for the purchase of coal from the Bel-Aire mine, we feel that it would be in the neighborhood of $100 million in additional costs to our customers. Again, that's not a hard-and-fast figure, and I prefer to get something more accurate in writing, too.

Senator **Grassley**. Is that $100 million into the future, throughout the life of the 25-year contract?

Mr. **Parkin**. Right.

Senator **Grassley**. How may years have you been into it?

Mr. **Parkin**. I believe it was 1979 or 1978.

Senator **Grassley**. In other words, the contract is almost simultaneous with the passage of this legislation?

Mr. **Parkin**. There are several million dollars being held right how in the trust account administered by the courts while the decision is being finalized.

Mr. **Purcell**. Senator, as stated in our testimony, approximately 59 percent of our electricity is generated by coal-fired plants. The bulk of the rest—in fact, about 40 percent of the rest of our electricity—comes from a contract we have with the Quad Cities Nuclear Stations, Cordova, IL.

I, too, am at a loss to quote a figure as to how much rate overcharges have cost our customers. But the obvious question is what those rates would be if they were at what we would term an equitable level. We are presently in the very preliminary stages of investigating the possibility of negotiating a carriage contract with Burlington Northern for our Wyoming coal, and if and when that contract is consummated, then I would be in a much better position to say how much we think the overcharges have cost our customers. But I'll try to get you a figure for the record.

Senator **Grassley**. Well, Jerry, that reminds me; the figure you gave me, then, is a study view by your corporate economist and accountants?

Mr. **Parkin**. This figure would not apply strictly to Iowa Power and Light Co., but to all of the owners of Council Bluff Unit No. 3. There are several other investor-owned utilities and generation and transmission co-ops that are partners there.

Mr. **Stoll**. Iowa Public Service Co., as far as our general organization, is 99-percent coal-fired, although we do, on occasion, buy energy through other systems, and I can't tell you what those are. But what we generate is 99-percent coal fired. I think in my testimony I indicated that we feel there's been about a $4 overcharge.

Senator GRASSLEY. $4 per month?

Mr. STOLL. $4 per ton, and that amounts to $8 million a year. We move about 2 million tons of coal a year on that unit. We've been on this rate since 1978, waiting for an agreement from ICC for a final determination.

Now, as far as Iowa Public Service Co., is concerned, we own approximately 40 percent of that plant. However, the balance of it is owned by other investor-owned utilities, municipalities, cooperatives in Iowa and South Dakota, so the full $8 million effect would be on utility customers, not just Iowa Public Service Co.

Mr. PITNER. Iowa Electric's contract for coal from Craig, CO, which utilizes the services of the Denver and Rio Grande, which is our only railroad available to that area, has cost us considerable excesses in freight charges, we feel. We have done a study with regard to that particular contract, and, while the savings we estimate to our customer is over the life of that contract and some other contracts we have—if we can break these down for you, Senator—but with that contract and another contract out of some other coal mines in Missouri, we estimated that we could save our customers, over a period of about 13 years, approximately somewhere around $200 million over a 13-year period by going to a spot market, if it were available. But I will firm those figures up for you.

Senator GRASSLEY. Along that line, I never thought of this until after Commissioner Varley left the table, so I might ask him at this point. He used an example of the Wisconsin utilities, where some of them ship entirely by train and then some ship by other means. Do you know of other examples where the costs are higher in one compared to the other, where there's more competition? Or was that news to you, too, when you heard that?

Mr. STOLL. I might comment on that. That is not news. I've heard about the Wisconsin study previously. I don't know of anything in Iowa, offhand.

Senator GRASSLEY. Oh, no; not in Iowa. I mean anyplace else in the Nation.

Mr. STOLL. I'm sure there are. Why don't you let me see what I can come up with, and get it to you for the record. I'd be happy to.

[The following was subsequently supplied for the record:]

(1) Verified statement of Ronald G. Wasson on behalf of Kansas City Power and Light Company dated May 15, 1985 before the Interstate Commerce Commission in Finance Docket 30700.

(2) Brief of Western Coal Traffic League date November 20, 1985 before the Interstate Commerce Commission in Finance Docket 30700 page 21 through 27.

Senator GRASSLEY. Commissioner Varley, let me ask you at this point, do you have any other examples, or is that about the only one that you've been able to come up with in regard to that, where it seems to be so clear cut?

Mr. VARLEY. I couldn't give the other examples just off the top of my head, but let me make it clear that this case we're talking about, the plant, I believe, buys high-sulfur coal. Now, the Louisa plant, even though it's fairly close proximity to the Mississippi River, burns western coal—low-sulfur coal—and there's very little barge traffic in Wyoming, so we really don't have that option, even though you'd be close to the river. There's no other possible way of bringing it in by barges if you buy low-sulfur coal outside the country somewhere and ship it here.

Senator **Grassley**. I'm not sure that I understand. Does that detract from the point you were trying to make, using the Wisconsin utilities as an example?

Mr. **Varley**. Not at all. The point I was trying to make was that, under the present implementation of the law, the railroads are actually encouraged to overcharge captive shippers to subsidize with other forms of transportation, where it may not even be economical; that, in fact, by underpricing a shipment of coal to plants that have an option, you actually can increase the total cost of transportation to society as a whole, and you do it on the backs of the people who are customers of captive shippers.

Senator **Grassley**. OK. Thank you. One of you on this panel made some sort of comment about the ICC having a prorailroad bias. I'd like to know why, in your opinion, you say that. According to your testimony, you indicated that S. 447 may not be the real solution to the problem, and so I have to ask, are you saying that the ICC, if it chose to deal with the problem, was interpreting the Staggers Act as it was originally intended? You may have made some mention of the prorailroad bias. Whether or not the two are connected, I still want you to comment as an expansion of your testimony. Did I misinterpret one of you?

Mr. **Parkin**. I think that was probably the general drift of all of us.

Senator **Grassley**. Well, I didn't think it was a general drift. I thought that somebody actually said so.

Mr. **Parkin**. I think we probably did.

Senator **Grassley**. Go ahead and comment.

Mr. **Parkin**. We feel that the ICC's interpretation of Staggers has been more to the interest of the railroads, and I think that probably goes to a certain degree because the ICC is used to dealing with railroads and the problems with railroads and the concerns of railroads. In that manner, they're more knowledgeable about the railroads and tend to view the railroad's interests a little differently than the rest of us do.

I think that their interpretation of the law could be different and could still protect the railroads, while also at the same time protecting the rights of the shippers. And some of those concerns that we've got are, for example, the revenue of adequacy determination, which is really an arbitrary formula that's contained in the law, that probably should be changed; market dominance, which we think could be improved. I think there are several points which could be improved, that might give the ICC some better direction on exactly what the intent of Congress was with this law.

Senator **Grassley**. Your statement makes me also ask, as a third part of the question, what's your alternative for going to the ICC?

Mr. **Parkin**. I'm not a lawyer, but I would imagine the alternative would be going to court after all the remedies of the ICC are exhausted.

Senator **Grassley**. Mr. Purcell?

Mr. **Purcell**. Senator, in the current interpretation of the Stagger's Act used by the ICC to prove market dominance, which is the first step the captive shipper has to take to get the ICC to take action to relieve what the shipper feels in an excessive rail rate, the shipper has the burden of proving, essentially—I am not an attorney, either, but what I understand are essentially all the elements of an antitrust case; that there is no intramodal competition; that there isn't any other form of transportation—barge or truck, in the instance of coal; that there isn't any geographic competition; that there isn't another source that the coal user, in this instance, could utilize.

In relying, then, on the antitrust statute to solve the problem of the captive shipper, it seems that you really are going around in circles a bit, because the captive shipper has to prove all the elements in the antitrust case anyway before the Interstate Commerce Commission, and that's only the first step they have to take. Once they have proven market dominance, they go on to prove that a rate is unreasonable, and only after that step is taken do they have to prove that a railroad is revenue inadequate.

Senator GRASSLEY. Let me suggest that maybe you'd have an unbiased judge, as opposed to a biased commission, in the case of going to court. I mean, you'd surely see that as a better position, right?

Mr. PURCELL. Yeah, if——

Senator GRASSLEY. You might see it as a better position, but is that the route you'd want to go?

Mr. PURCELL. I guess the main problem with the antitrust route is the time it takes to ultimately receive a decision.

Senator GRASSLEY. I think we on the Judiciary Committee and in Congress need to be reminded of that once in awhile. Mr. Stoll?

Mr. STOLL. I might comment there, as far as the timing on it. Our rate case, even, at the ICC, where we had gone to the ICC, started in 1978, and we're still waiting. That's 7 years. We have gone into the courts, and we got a decision in less than a year out of the ICC, but then both ourselves and the railroad appealed to the court, and it went back, and the ICC has been basically sitting on it. We filed recently, I hope, the final filing that we have to make in anticipation of decision, but that's been 7 years just trying to go through the regular court process.

Senator GRASSLEY. Mr. Pitner, do you have anything to add?

Mr. PITNER. Yes, Senator. I think that the delay that's occurred when you get to the court process does not make relief timely when, in fact, we would prefer that if the interpretation process by ICC were accomplished, it would happen contemporaneously with your needs, and that's why we prefer the Staggers Act amendments. I might just refer you to the Iowa-Illinois statement, and I might just read a paragraph to answer your question.

Senator GRASSLEY. Please do.

Mr. PITNER. Under current law, even if the ICC finds that a captive shipper is being charged an unreasonable transport rate, the agency cannot order a railroad transport rate, the agency cannot order a railroad to reduce that rate unless it finds that the railroad is revenue adequate. So even though it's unreasonable, under the standard for this revenue adequacy test currently being used by the ICC, that agency has never, in the 5 years since Staggers was enacted, found a railroad to be revenue adequate. These findings have produced anomalies like that of Norfolk Southern, which recently purchased North American Van Lines for $315 million and has made a much publicized offer of $1.2 billion for Conrail, being found to be revenue inadequate by the ICC.

I think that is a very graphic statement of some of the problems we have with the ICC interpretation.

Senator **Grassley**. There's a point made by the railroads that S. 447 subjects them to the antitrust laws with respect to an area, and regulation by the ICC. Would you agree to the abolishment of the Interstate Commerce Act and subjection of the railroads to the full reach of the antitrust laws in the same manner as other industries? I'd like your comment.

Mr. **Parkin**. I don't know. That's something that would take a heck of a lot more study than I could give in 1 or 2 minutes right now.

[The following letter was subsequently supplied for the record:]

IOWA POWER
666 Grand Avenue
P O. Box 657
Des Moines, Iowa 50303
515-281-2900

September 4, 1985

The Honorable Charles Grassley
U.S. Senate
135 Hart Building
Washington, D.C. 20510

Dear Senator Grassley:

During your hearing on August 29 in Waterloo, you asked that I submit information for the record regarding the current coal hauling rate dispute between Iowa Power and Light Company, along with the other owners of Council Bluffs Power Station Unit # 3 (CB # 3), and the Burlington Northern (BN). Following is that information.

From November 1, 1981 through December 22, 1983, the owners of CB # 3 paid the Burlington Northern approximately $15 million, including interest, in excess of the contract rate on shipments of 4.3 million tons of coal from Gillette, Wyoming to Council Bluffs, Iowa. This dispute arose because the BN claimed that a signed letter of agreement for shipping costs was not a binding contract - a matter that Iowa Power and the other CB # 3 owners obviously disputed. These disputed funds have been held in escrow pending the outcome of litigation with the BN.

We have prevailed in part of this litigation involving coal shipped from the Belle Ayr mine in Gillette, thereby saving our customers close to $40 million over the next several years. We are scheduled to be in the U.S. District Court on December 9 of this year on the argument that our contract rate with the BN also applies to coal shipped from the Eagle Butte mine in Gillette. Should we prevail on this argument, our customers will be saved an additional $37 million.

If Iowa Power and the other CB # 3 owners had not challenged the BN on their shipping costs, electric customers in Iowa would have seen an unnecessary expenditure of over $100 million over a twenty year period.

I hope this information is helpful.

Sincerely,

Jerry D. Parkin
Manager, Government Affairs

Senator **Grassley**. Do any of you?

Mr. **Purcell**. I guess, Senator, I disagree with the premise of your question, which I take it is the premise that's used by the railroads——

Senator **Grassley**. Yes.

Mr. **Purcell**. That the legislation we support would return them to a regulatory system. Under the legislation we support S. 447 only those captive shippers who could prove market dominance and prove that their commodity is captive to a single railroad, would be able to use the ICC regulation. Those railroads which serve shippers who are not captive would not have to come under the ICC regulations, so I'd take issue with that premise.

Senator **Grassley**. I see.

Mr. **Pitner**. I guess especially in our area, in Iowa, with the mergers of railroads and abandonment of lines by Rock Island and Milwaukee and the questionable status of Iowa being served because of such a low market, that the railroad industry tends to stay as a monopoly situation in our area. I'm not sure monopoly business really does well as a market-related and market-free business, in a monopoly situation; and therefore, opening up to the Sherman antitrust actions and acts of Congress isn't necessarily the most timely relief that we can get out of a monopoly situation. I think it has to be before a regulatory agency.

Senator **Grassley**. On another point, a lot of the witnesses that we've had in Washington have testified that 447 is preferable to 477; 477 is the one that revises the Staggers Act. And the reason they've said this is that 477, in the current deregulatory environment—and I suppose it depends on whether you believe that that's a good environment—would reregulate the market, rather than promoting competition, which was the goal of the Staggers Act. I'd like to have your comments on that.

Mr. **Stoll**. There, Senator, I don't think it's the intent of 477 to reregulate. We're talking about and only about the captive shippers. We're not talking about the other people that happened to have access to the railroads. We're talking only about captive shippers, and our feeling is that the Staggers Act actually gave us that protection, but it's not being interpreted in that way by the ICC, and it does not appear that the ICC is going to interpret it that way. And we need Congress to give us that assistance.

Senator **Grassley**. Any further comment by the other three of you?

Mr. **Pitner**. In the attempt to deregulate—and we're certainly supportive of that where natural monopoly indices are not present—but in our area in Iowa, it seems to me that we have more monopolistic tendencies than we do an open market; and therefore, open access is not available. Therefore, there has to be a transitional period.

Senator **Grassley**. I wonder if there can be any quantifying of how much of the rail market is captive? I mean, we've talked here about grain and about utilities, but have you ever run across anything that would quantify the total amount of all railroad transportation that would fall in the captive shippers? I suppose that would be difficult to do.

Mr. **Pitner**. I think we can make an attempt at that, Senator.

Senator GRASSLEY. I'd appreciate that. I have no further questions. Do any of you have anything, in the way of closing or summary, a point that you haven't had a chance to make yet? OK. Thank you very much.

Our next panel consists of Bob Stone, who's general manager of physical distribution of Terra Chemicals International in Sioux City; Ken Ludlow, executive director of Iowa Grain and Feed Association in Des Moines; Richard Crom, general manager of Walnut Grove Products in Atlantic; Don Crane, who is a consultant with W.R. Grace Co. in Washington, DC; and Terry Voss.

I don't know how we're going to get all five of you up here, but let's see if we can do that. Terry Voss is president of United Purchasers Association in Des Moines.

So, would Mr. Stone start out, please.

STATEMENT OF PANEL CONSISTING OF: BOB STONE, MANAGING DIRECTOR OF PHYSICAL DISTRIBUTION, TERRA CHEMICALS INTERNATIONAL, SIOUX CITY; KENNETH L. LUDLOW, EXECUTIVE DIRECTOR, IOWA GRAIN AND FEED ASSOCIATION, DES MOINES; RICHARD L. CROM, GENERAL MANAGER, WALNUT GROVE PRODUCTS, ATLANTIC, IA; DONALD A. CRANE, CONSULTANT, W.R. GRACE CO., WASHINGTON, DC; AND TERRY J. VOSS, PRESIDENT, UNITED PURCHASERS ASSOCIATION, DES MOINES, IA

Mr. STONE. Yes, Senator. I do not intend to read my statement. I do appreciate the opportunity to express my views, my company's views, and those of the fertilizer industry. Essentially, the fertilizer industry is supportive of S. 447.

A little about myself and my company: Terra Chemicals is a manufacturer and distributor of fertilizers, feed ingredients, and crop protection chemicals. We operate in a 22-State area, where we own and operate 227 retail plants. As a farmer yourself, you realize that there's three basic plant nutrients: nitrate, phosphate, and potash. Most of the nitrate production is located near a natural gas supply. Most nitrogen-based fertilizer companies have the advantage of having barge competition, pipe competition, and truck competition. For example, there are a number of nitrogen plants located right in the State of Iowa, which can serve the farmer customers on a truck basis. However, phosphates and potash are quite rail dominant and captive to rail, in that phosphates predominantly are originated in central Florida, Bone Valley area.

Potash, originating in central Canada, is also rail dominant, in that there is no other mode of transportation available.

The State of Iowa ranks third nationally in fertilizer consumption. It represents about 8 percent of the Nation's fertilizer usage is used in the State of Iowa. And of the price that the farmer pays for fertilizer, 30 to 40 percent of that is transportation expense. Those are based on national averages, and I would almost estimate that Iowa may be a little higher, because it's about as far as you can get from Canada and Florida. But on a national average, 30 to 40 percent of the price a farmer pays for fertilizer is transportation.

One of our main concerns is that with the passage of the Staggers Act, nitrogen-producing companies, such as Terra, were able to benefit. We actually benefited from deregulation and are in favor of deregulation. The railroads, when the Staggers Act was passed, kind of made a wholesale effort to reduce rates where competition existed. They were trying to secure traffic that was off rail. They were going out and attempting to secure traffic from the barge lines, the pipeline, and the truck lines. One of the witnesses earlier alluded to that, and I've heard it called predatory pricing.

So our position is that where there is competition, there is at least an alternative and a way to keep rates at a reduced level. Our concern is that on the potash and phosphate, there is no competition. The rails have it.

We feel that this piece of legislation, by subjecting the railroads to the antitrust laws, would allow us to at least maintain what little competition we have now. We feel that it also would be helpful in promoting additional competition. And the competition I'm talking about is rail-to-rail competition. Currently, the railroads have the ability to determine who they will do business with and who they won't do business with, including each other. By cancellation of joint rates and through routes, a carrier that's serving a particular origin can assure himself of his long haul and basically minimize or reduce the number of carriers that would participate in that movement. And what we are really looking for is something that would allow us to have as much rail-to-rail competition as possible, and we feel that this piece of legislation will give that to us.

Mergers have been a big factor in eliminating rail-to-rail competition. I personally feel that one of the reasons a number of these mergers are taking place is that the carriers can see the power to monopolize a specific market. I feel that this piece of legislation would allow or give the shipper some alternatives. The key to the whole success of maintaining rate levels as they currently are and guarding against excessive increases and even promoting decreases is competition. Where there's competition, we have had some successes, and where there is no competition, it's whatever the market will bear, and we're at the mercy of the carriers.

The State of Iowa, as I mentioned, consumes about 8 percent of the Nation's fertilizer. It's estimated, using national averages, that the transportation bill that the Iowa farmer pays is in the neighborhood of $300 to $400 million per year. A large portion of that, I feel, can be reduced by providing effective competition, specifically on the potash and the phosphates. We feel that this bill will do it, and therefore ask your support or your sponsorship or whatever it will take to get this piece of legislation passed. Thank you.

[The prepared statement follows:]

Statement of
BOB STONE
Terra Chemicals International

on behalf of
THE FERTILIZER INSTITUTE

Thank you, Chairman Grassley for inviting me to appear at your hearing today.

My name is Bob Stone. I am Managing Director, Physical Distribution for Terra Chemicals International, Inc., headquartered in Sioux City, Iowa. I appear here today on behalf of The Fertilizer Institute* as I am a member of the Institute's Transportation Committee.

Terra Chemical International, Inc. was organized in 1964. The company is a manufacturer and distributor of fertilizers, feed ingredients and crop protection chemcials. Primary product facilities are located at the Port Neal Industrial Complex near Sergeant Bluff, Iowa, a few miles south of corporate headquarters in Woodbury County, Iowa. Additional manufacturing facilities are located at Woodward, Oklahoma.

Terra produces nitrogen based fertilizers at its two manufacturing locations. These products include anhydrous ammonia, nitrogen fertilizer solution, urea, ammonium nitrate and nitrogen feed supplements. Terra owns and operates 277 Retail outlets in 22 Midwestern states. These Retail locations provide a full line of fertilizer and crop protection chemicals to their farmer customers. Terra supplies these locations with its own produced nitrogen product and with purchased potash and phosphate material.

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*TFI is a voluntary, non-profit association, whose members represent approximately 95 percent of the domestic fertilizer production in the United States. TFI's membership includes: producers, manufacturers, traders, retailer dealers and distributors of fertilizer materials. Its members are major shippers, receivers, and exporters of fertilizer and fertilizer materials and are a vital link in the nation's agriculture system.

Terra employs approximately 1600 employees throughout its 22 state marketing area. Terra employs 400 in the state of Iowa. Terra's annual net sales in 1984 were $374 million and it is anticipated that our net sales for 1985 will be $631 million.

The fertilizer industry strongly supports concepts embodied in S. 447. We agree completely that the application of the antiturst laws to the railroad industry is the next logical step in the steady, bipartism process of deregulatimg the nations railroads. With passage of the 4R Act of 1976 and the Staggers Rail Act in 1980, Congress freed the railroads to operate in the same manner as unregulated business in the general economy with market forces determining railroad rates and activities. Thus, it seems to the fertilizer industry that Congress should also determine whether, in today's deregulatory environment, the railroad industry should be made fully subject to antitrust laws to protect and promote railroad transportation competition. Thus, we urge you, Mr. Chairman, to support the objectives S. 447 attempts to achieve.

Unlike most of the American commercial world, the railroad industry does not have to be concerned with private suits for price fixing, monopolization or attempts to monopolize. Private suits for price fixing or monopolization against railroads stopped in 1922 when the Supreme Court held in Keogh v. Chicago and Northwestern Railroad, 260 U.S. 156, that railroads were immune from damage awards under the Sherman Act because of ICC jurisdiction over rail rate regulation. In addition, by statute, injunction actions by private parties against railroads under any of the antitrust laws are not permitted because Section 16 of the Clayton Act expressly prohibts such actions against ICC regulated carriers accept by the Department of Justice. Thus, the Interstate Commerce Act allows railroads to enjoy certain exemptions to the antitrust laws.

These exemptions are most noticeable when railroads take anticompetitive action to keep traffic on their long-haul routes, a practice that even railroad executives recognize. John W. Snow, President of Chessie System Railroads, in testimony March 27, 1985 before the Senate Judiciary Committee on the Antitrust Implication of the Sale of Conrail to the Norfolk Southern Corporation stated:

> "Railroads traditionally seek to reroute traffic over their long-haul routes. As long as competitive alternatives are available, this practice is generally desirable, and benefits shippers. But where one system controls both the origin and the destination of the traffic, the results are exetremely harmful. A railroad with that kind of control gains a dominant position over customers and competing railroads too." (Emplasis added)
>
> ". . .Only those shippers open to competitive rail service at both the origin and destination points of their movements will be able to avoid the monopolizing grip of the NS-Conrail combination."

Two significant anticompetitive trends that increase railroad monopolizing grip over situations where they control the origin and destination of the traffic are in the area of joint rates and reciprocal switching arrangements. Without going into excessive detail, joint rates and reciprocal switching arrangements are means by which railroads have eliminated competition. In regard to joint rates, suppose Railroad X offered single line service between points A and C, while Railroad Y only served point C but could connect with Railroad X at intermediate point B.

Traditionally, Railroads X and Y would offer a joint rate between points A and C that would be competitive with Railroad X's single line rate and which would be lower than the combination of rates between points A and B and between points B and C:

```
_________Railroad X__________B _ _ _ _ _ Railroad Y_ _ _ _ _ _ _ _
A                                                                C

__________________________________________________________________

                        Railroad X
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In regard to reciprocal switching, suppose a particular shipper's plant (P) is located on the tracks of a particular railroad (X). Railroads X and Y would negotiate reciprocal switching arrangements that permitted Railroad Y access to the plant.

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_ _ _ _Railroad Y_ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _ _
A                        +                                       C
                         +
_________________________+  (+++ = Access to P via switching)_____
       Railroad X
```

In turn, Railroad Y would permit similar access to Railroad X at another plant.

The result of joint rates and reciprocal switching arrangements provided competitive alternatives for the shipper. The shipper whose origin and destination are controlled by one railroad is not totally limited to the use of the services of a single carrier. Unfortunately, beginning around 1982 and continuing to the present day, many of the Nation's largest rail carriers have been unilaterally -- and on a wholesale basis --

cancelling joint rates[1] and cancelling or restricting reciprocal switchng arrangements[2] in those situations where the cancelling carrier can perform the service single line. Many fertilizer and other agricultural shippers have been affected severely by these practicees, as there are many routes where now only a single carrier can perform the single line service. Each cancellation, in turn, further decreases the number of routes where competition previously had been available. This has resulted in the growth of railroad monoploy power and the need for complete deregulation of the railroad.

The fertilizer industry supports the concepts in S. 447 because it attempts to provide shippers competitive rail service at both the origin and destination points and prevents railroads from exercising monopoly power provided in certain cases by deregulation.

The following is a specific example in the fertilizer industry where control over the origin gains a dominant anticompetitiveness position over the shipper and competing railroads in a long-haul route.

In the Bone Valley of Central Florida, the phosphate industry mines and processes 50-60 million tons a year of phosphate, an essential ingredient in fertilizer. Bone Valley desposits are 80 percent of the U.S. supply of, and one third of the world's demand for this irreplaceable component in our food chain. There are 21 phosphate rock mines and 11 mine owners in the Bone Valley but only one railroad -- the Seaboard System Railroad -- which serves the area with an average of 44 phosphate trains a day.

The Seaboard transports approximately 90 percent of all phosphate tonnage moving to Tampa Port where both origin and destination are served by rail and 98 percent of all phosphate tonnage originating in the Bone Valley to interior U.S. points. Phosphate products rank second or third behind coal on the list of commodities which generate revenue for the Seaboard Railroad System -- in the neighborhood of $100,000,000.

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[1] E.g., ICC Docket No. 39176, The Chlorine Institute, Inc. v. The Atchinson Topeka & Santa Fe Ry. Co., et al.

[2] Id.

The closest rail competition to the Bone Valley -- to the Seaboard System Railroad -- is approximately 200 miles away, where the Norfolk Southern -- in competition with the Seaboard -- serves the Jacksonville, Florida area.

The Jacksonville Gateway to the Southern Railroad, was for years a competitive tool used by phosphate producers in negotiations with the Seaboard. However, shortly after the Staggers Act became law -- the Seaboard closed the Jacksonville gateway with the Southern thereby eliminating that rail completition. This action eliminated for phosphate producers, a competitive negotiation tool, and denied them the opportunity to enter into contracts with the Southern for phosphate tonnage originating out of the Bone Valley.

Such action is clearly in violation of the spirit of the antitrust laws, however, as stated, shippers are prohibited from seeking injunctive relief against such action nor can they seek trible damage for economic injury resulting from the anticompetitive action.

Mr. Chairman, we at Terra Chemicals individually support S.447 because the eliminations of joint rates and routes have already affected our business and could conceivably impact it much greater. Terra annually markets approximately 125,000 tons of phosphates in our marketing area. Because of the Seaboard System's monopolistic stronghold over Florida movement, our ability to negotiate rail rates is virtually non-existent. Terra's movements are to our retail outlets in railcar quantities or river terminals by barge thence truck to destination. Without adequate rail competition, the rail movement is captive since barge/truck movement is currently being optimized.

Terra's product facilities at Sergeant Bluff, Iowa and Woodward, Oklahoma are both local on the Chicago Northwestern and Santa Fe Railroads respectfully. Currently, there have been joint rate or route cancellations that have adversely affected us but if the Chicago Northwestern were to cancel routes and rates currently in effect at Sious City or if the Santa Fe cancelled routes and rates over Deming, NM, Terra could be extremely restricted in its ability to negotiate rates with competing carriers. We currently have contracts with the BN over the Sioux City route and with the SP over the Deming route.

In summary, we applaud you, Chairman Grassley, for holding these hearings to closely examine the antitrust laws and their underlying principles with respect to their application to the railroad industry. We believe the thrust of S. 447 is positive and legislation like it is absolutely essential to assure railroad transportation competition. We urge your support.

Senator GRASSLEY. Mr. Ludlow—Ken, I should say. I've known you long enough to call you Ken.

Mr. LUDLOW. Thank you, Senator.

Senator GRASSLEY. I know you from the years I was in the legislature.

STATEMENT OF KENNETH L. LUDLOW

Mr. LUDLOW. Thank you for asking me to appear here. And I'd like to tell, for the record, I'm not a traffic expert, nor do I purport to be a true student of the Staggers Act, so what you see before you is a reflection of the average country elevator shipper.

The complexity of the act and the complexity of remedies for the country shipper and, indeed, the grain trade have led to a basic feeling of apathy on the part of country elevator shippers. I'm talking about the midsize and the small shippers. We have held conferences on the act and have included talks on the act in our convention and meeting programs, and I've just completed a contracting seminar which Mr. Voss' organization cosponsored, along with AGRI-Industries, and we attracted a standing-room-only crowd, but only had about five country elevators show up.

The first question, of course, is why does this apathy exist on the part of the elevator, which I think I answered in the preceding paragraph. When such subjects as market dominance, contracts, demand-sensitive rates, compensatory joint rate relief, reciprocal switching, and so forth are brought up, the usual reaction of the country elevator is unanimous and predictable. He says, "What can I do about it?"

As a result, the country elevators have simply left it to their regional marketing cooperatives or their major national-international grain trading companies to protect their interests in these many areas since, and perhaps mistakenly, they feel their interests are as vital as theirs; and thus, any steps to be taken will be taken by them. Iowa Grain & Feed itself does not have the expertise nor, more importantly, the money to pursue remedies in depth. The issue before us, S. 477, is extremely important to Iowa, despite what many call the blessing of different modes of transportation and the truck connections to both rivers. Now, a very high percentage of Iowa's grain moves by rail, not only inter but intrastate as well, since some carriers have moved dramatically to meet truck competition. The second factor is that the Iowa rail structure now is relatively concentrated to serve the high grain exporting counties of Iowa. Also, the river terminals cannot serve the industry during the winter months, and it is at this time that Iowa grain shippers truly become captive to rail movement or truck movement into processing centers such as Cedar Rapids and, to a lesser extent, Des Moines and Council Bluffs-Omaha.

Now, I must admit some confusion on my part with the wording of the act and what is the general practice of railroads in regard to cancellation of joint rates and routes when I read the language in 49 U.S.C. 10705, which states, "Nothing in this subsection shall be construed to limit the authority of the commission under Section 10705(a) of this title to prescribe joint rates which provide a rail carrier participating in such joint rate revenues equal to or greater than 110 percent of its variable cost of providing service over each route to which such rate applies."

Now this, coupled with any evidence a shipper may present which proves to the Commission that the shipper has no competitive alternative and that the revenue to the canceling carrier is at least 110 percent of its variable costs, should be a remedy. It should clear the situation up.

But alas, herein lies the problem. Who is to initiate the action to find out if the revenue to the canceling carrier is 110 percent, as stated above, and that he has no competitive alternative?

Now, perhaps Senate 477 is the answer, but for the country elevator system, we wonder if it's the most practicable answer.

I want to quote one witness that appeared about 2 years ago before the Senate Subcommittee on Surface Transportation, when he said that "The antitrust laws are no protection to most of the shipping public. They are not designed to deal with the types of abuses which are prevalent in the railroad industry today.

"Second, only the wealthy can afford to invoke them. Where antitrust laws could have helped was in preventing anticompetitive mergers of railroads which have made possible the wholesale closing of competitive routes."

Now, I don't know if I agree with him wholeheartedly in everything he said, but I do think that he brings up a very important point. The invocation of antitrust proceedings brings to us a picture of money and time. And in the grain industry, time itself is a monumental element of antitrust litigation.

Now, the ability of any carrier to cancel, without justification, joint rates through routes and reciprocal switching, however, must be brought under control, whether through the antitrust laws or meaningful amendments to the Staggers Act which will compel, without question, the Commission to ascertain whether or not the action is justified.

Senator, I want to digress just a minute now. If you would go out into the country and visit a country elevator and maybe attend many of the meetings that we put on and the district meetings and so forth, I think rightly or wrongly, the feeling of the country elevator—the first receiver in the distribution of grain—that they feel the Interstate Commerce Commission has said, "you have passed the act, but we will administer it." Now, that's an elemental truth, of course, but what they really are saying is that they're ignoring you and ignoring the intent of Congress and I think that this goes much deeper than even the situation we're discussing right here.

Now, I'd like to shift this situation back to the originating end of grain to impress upon you the necessity of this or like legislation. At Clear Lake, IA, two country elevators have no competitive access to Cedar Rapids, IA, due to their inability to negotiate a reasonable switching arrangement that would result in access to a carrier that does serve Clear Lake and also does serve Cedar Rapids. Now, their present rate is 24 cents. If they could switch over to the other line, their rate would be 11 cents. Now, moreover, one of the elevators specializes in merchandising waxy corn for the area farmers, and they're forced to rely primarily on an eastern market, rather than a more lucrative west coast market. Now, all this is for the same reason, because of no reciprocal switching available over to the other line.

Now, I'm sure you're aware, too, that in many cases the switching charge on the destination side has been taken out of the linehaul rate and placed in separate tariffs and switching tariffs at an exorbitantly high rate which effectively cancels the rate, as well.

Now, I would be remiss at this time if I did not venture for a moment into another area of Staggers that is, again, without remedy for most country elevators. This is contracting, which is becoming more prevalent in the grain industry, but due to disclosure rules of the Commission, forces the country elevator to subscribe to contract reporting services to even know when he is being undercut before it's too late.

Now, the usual situation is that the smaller and the midsize country elevators are not even aware of a competitive situation created by a contract until it is too late to do anything about it. With the Commission now automatically granting an immediate effective date, this further emasculates the intent of Staggers, which was first understood to grant a 30-day effective date period.

Now, when a shipper does become aware that most of his business is going crosss-country, he then has to initiate an action within the 30-day period and file a complaint, which includes requesting discovery of second-tier contract terms. If he is successful in proving unreasonable discrimination, he may find that a similar contract, that he now has the right to, has been filled by a particular agreement or contract, perhaps entered into by his competitor and an individual processor or terminal point. And he is thus left in the unenviable position of either having his original grain merchandising area depleted or unable to ship to the destination due to the destination perhaps being co-contractors.

In finality, however, the legal and traffic management expertise needed to litigate an alleged discriminatory contract situation is beyond the financial resources of most grain shippers.

In conclusion, perhaps Senate 477 is an appropriate vehicle, but there are doubts raised as to whether or not the antitrust acts are the vehicles to use.

I won't read my closing statement. You can read it at your leisure, Senator, but it is a favorite quote from a favorite act of mine. I want to also point out something about the Commission and the method and the manner in which it acts.

In December 1983, the Second Circuit Court in New York found partially on behalf of the grain industry and the fertilizer industry and in regard to second-tier discovery, to get right down to the elements of a basic contract. Now here it is just about September 1 of 1985. They are still operating under interim rules that have been adopted according to the court order, but actually the interim rules suggested no real relief from the original rules. Now, it's this malaise or whatever you want to call it—we're coming up on 2 years since the court said, "You are wrong, Commissioners, and you should be doing this." And this is just, I think, one element. As far as antitrust is concerned, I think maybe Iowa Grain and Feed Association would say we're the State association—we have to take the blame for not helping these country shippers, but with over 900 country elevator members, we can't do this.

And second, it was brought out at our last contracting conference that we might be in trouble with antitrust even doing this. And then the small and midsize country elevators also are looking at antitrust as a possible violation of law on their part if they would try to pool and, say, go together and negotiate a contract rate. Now this also was brought out during our last seminar on contracts. So actually, I think it was suggested at that time that if you did have some of the smaller elevators that wanted to compete with a larger elevator, that they should actually submit—I forget what the actual legal term is—a synopsis or a statement to Justice to tell what they would intend to do with it. Then Justice would come back and say, "Yes, you are in violation of antitrust" or "No, you aren't."

So I think that something has to be done, really, and perhaps this is the vehicle to do it, as I said before. But I really have serious doubts in my own mind whether or not antitrust is the way to do it. Thank you very much.

[The prepared statement follows:]

igfa
iowa grain and feed association
2882 106th Street, Des Moines, Iowa 50322 / (515) 278-0086 / Telex 439-088 IGFA-DMS

STATEMENT OF KENNETH L. LUDLOW, EXECUTIVE DIRECTOR
IOWA GRAIN AND FEED ASSOCIATION
BEFORE THE FIELD HEARING OF THE SENATE SUBCOMMITTEE
ON ADMINISTRATIVE PRACTICE AND PROCEDURE
OF THE SENATE COMMITTEE ON THE JUDICIARY
RE S.477, AN ACT TO AMEND THE SHERMAN ACT
WATERLOO, IOWA, AUGUST 29, 1985

THANK YOU FOR THE OPPORTUNITY TO APPEAR HERE TODAY. MY NAME IS KENNETH L. LUDLOW AND I AM EXECUTIVE DIRECTOR OF THE IOWA GRAIN AND FEED ASSOCIATION, 2882 106th ST., DES MOINES, IOWA 50322.

FIRST, I WOULD LIKE TO INFORM YOU THAT I AM NOT A TRAFFIC EXPERT NOR DO I PURPORT TO BE A TRUE STUDENT OF THE STAGGERS ACT BUT IN DOING SO PERHAPS YOU WILL SEE A REFLECTION OF THE AVERAGE COUNTRY ELEVATOR SHIPPER AND HIS RELATIONSHIP TO THE ACT.

THE COMPLEXITY OF THE ACT AND THE COMPLEXITY OF REMEDIES FOR THE COUNTRY SHIPPER, AND INDEED THE GRAIN TRADE, HAVE LED TO A BASIC FEELING OF APATHY ON THE PART OF COUNTRY ELEVATOR SHIPPERS. WE HAVE HELD CONFERENCES ON THE ACT, HAVE INCLUDED TALKS ON THE ACT ON OUR CONVENTION AND MEETING PROGRAMS AND HAVE JUST CONCLUDED A CONTRACTING SEMINAR IN DES MOINES WHICH ATTRACTED A STANDING ROOM ONLY CROWD BUT WITH ONLY 5 COUNTRY ELEVATORS ATTENDING.

THE FIRST QUESTION, OF COURSE, IS WHY DOES THIS APATHY EXIST ON THE PART OF THE ELEVATOR AND I THINK I ANSWERED THAT IN THE PRECEDING PARAGRAPH. WHEN SUBJECTS SUCH AS MARKET DOMINANCE, CONTRACTS, DEMAND SENSITIVE RATES, COMPENSATORY JOINT RATE RELIEF, RECIPROCAL SWITCHING, ETC., ETC., ARE BROUGHT UP THE USUAL REACTION OF THE COUNTRY ELEVATOR IS UNANIMOUS AND PREDICTABLE - WHAT CAN I DO ABOUT IT?

AS A RESULT, THE COUNTRY ELEVATORS HAVE SIMPLY LEFT IT TO THEIR REGIONAL MARKETING COOPERATIVES OR THEIR MAJOR NATIONAL/INTERNATIONAL GRAIN TRADING COMPANIES TO PROTECT THEIR INTERESTS IN THESE MANY AREAS SINCE, AND PERHAPS MISTAKENLY, THEY FEEL THEIR INTERESTS ARE AS VITAL AS THEIRS AND THUS ANY STEPS TO BE TAKEN WILL BE TAKEN BY THEM. IOWA GRAIN AND FEED ITSELF DOES NOT HAVE THE EXPERTISE NOR MORE IMPORTANTLY THE MONEY, TO PURSUE REMEDIES IN DEPTH THAT WE FEEL ARE ENDEMIC WITH THE GRAIN TRADE AND PRESENT TRANSPORTATION REGULATION.

THE ISSUE BEFORE US, S.477, IS EXTREMLY IMPORTANT TO IOWA DESPITE WHAT MANY CALL THE "BLESSING" OF DIFFERENT MODES OF TRANSPORTATION AND THE TRUCK

CONNECTION TO BOTH THE MISSIPPI AND MISSOURI RIVER TERMINALS. A VERY HIGH PERCENTAGE OF IOWA'S GRAIN MOVES BY RAIL, NOT ONLY INTERSTATE BUT INTRA-STATE AS WELL SINCE SOME CARRIERS HAVE MOVED DRAMATICALLY TO MEET TRUCK COMPETITION. THE SECOND FACTOR IS THAT THE IOWA RAIL STRUCTURE NOW IS RELATIVELY CONCENTRATED TO SERVE THE HIGH GRAIN EXPORTING COUNTIES OF IOWA. ALSO, THE RIVER TERMINALS CANNOT SERVE THE INDUSTRY DURING THE WINTER MONTHS AND IT IS AT THIS TIME THAT IOWA GRAIN SHIPPERS TRULY BECOME CAPTIVE TO RAIL MOVEMENT OR TRUCK MOVEMENT INTO PROCESSING CENTERS SUCH AS CEDAR RAPIDS AND TO A LESSER EXTENT DES MOINES AND COUNCIL BLUFFS/OMAHA.

I MUST ADMIT SOME CONFUSION ON MY PART WITH THE WORDING OF THE ACT AND WHAT IS THE GENERAL PRACTICE OF RAILROADS IN REGARD TO CANCELLATION OF JOINT RATES AND ROUTES WHEN I READ THE LANGUAGE IN 49 USC 10705 WHICH STATES, "(6) NOTHING IN THIS SUBSECTION SHALL BE CONSTRUED TO LIMIT THE AUTHORITY OF THE COMMISSION UNDER SECTION 10705(a) OF THIS TITLE TO PRESCRIBE JOINT RATES WHICH PROVIDE A RAIL CARRIER PARTICIPATING IN SUCH JOINT RATE REVENUES EQUAL TO OR GREATER THAN 110 PERCENT OF ITS VARIABLE COST OF PROVIDING SERVICE OVER EACH ROUTE TO WHICH SUCH RATE APPLIES."

THIS, COUPLED WITH ANY EVIDENCE A SHIPPER MAY PRESENT WHICH PROVES TO THE COMMISSION THAT THE SHIPPER HAS NO COMPETITIVE ALTERNATIVE AND THAT THE REVENUE TO THE CANCELLING CARRIER IS AT LEAST 110% OF ITS VARIABLE COSTS, SHOULD SIMPLY CLEAR UP THE SITUATION.

BUT, ALAS, HEREIN LIES THE PROBLEM. WHO IS TO INITIATE THE ACTION TO FIND OUT IF THE REVENUE TO THE CANCELLING CARRIER IS 110% AS STATED AND THAT HE HAS NO COMPETITIVE ALTERNATIVE?

PERHAPS S.477 IS THE ANSWER BUT FOR THE COUNTRY ELEVATOR SYSTEM WE WONDER IF IT IS THE MOST PRACTICABLE ANSWER. ONE WITNESS BEFORE THE SENATE SUBCOMMITTEE ON SURFACE TRANSPORTATION STATED SOMETHING THAT HAS CONCERNED ME FOR SOME TIME. HE SAID, "THE ANTITRUST LAWS ARE NO PROTECTION TO MOST OF THE SHIPPING PUBLIC......THEY ARE NOT DESIGNED TO DEAL WITH THE TYPES OF ABUSES WHICH ARE PREVALENT IN THE RAILROAD INDUSTRY TODAY. SECONDLY, ONLY THE WEALTHY CAN AFFORD TO INVOKE THEM. WHERE ANTITRUST LAWS COULD HAVE HELPED WAS IN PREVENTING ANTI-COMPETITIVE MERGERS OF RAILROADS WHICH HAVE MADE POSSIBLE THE WHOLESALE CLOSING OF COMPETITIVE ROUTES....."

I DON'T KNOW IF I AGREE WITH HIM WHOLEHEARTEDLY OR NOT, OR THAT I AM QUALIFIED TO DO SO, BUT THE INVOCATION OF ANTI-TRUST PROCEEDINGS BRINGS TO US A PICTURE OF MONEY AND TIME AND IN THE GRAIN INDUSTRY TIME ITSELF IS A MONUMENTAL ELEMENT THAT COULD NEGATE THE TIME CONSUMING PROCESS OF ANTI-TRUST LITIGATION.

THE ABILITY OF ANY CARRIER TO CANCEL, WITHOUT JUSTIFICATION, JOINT RATES, THROUGH ROUTES AND RECIPROCAL SWITCHING, HOWEVER, MUST BE BROUGHT UNDER CONTROL WHETHER THROUGH THE ANTI-TRUST LAWS OR MEANINGFUL AMENDMENTS TO THE STAGGERS ACT WHICH WILL COMPEL, WITHOUT QUESTION, THE COMMISSION TO ACT ON BEHALF OF SHIPPERS IN A METHOD OF DISCOVERY TO ASCERTAIN WHETHER OR NOT THE ACTION IS JUSTIFIED.

I WOULD LIKE TO SHIFT THIS SITUATION BACK TO THE ORIGINATING END OF GRAIN TO IMPRESS UPON YOU THE NECESSITY OF THIS OR LIKE LEGISLATION. AT CLEAR LAKE, IOWA, TWO COUNTRY ELEVATORS FOR ALL INTENTS AND PURPOSES, HAVE NO COMPETITIVE ACCESS TO CEDAR RAPIDS, IOWA, A MAJOR PROCESSING POINT IN IOWA, DUE TO THEIR INABILITY TO NEGOTIATE A REASONABLE SWITCHING ARRANGEMENT THAT WOULD RESULT IN ACCESS TO A CARRIER SERVING CLEAR LAKE THAT DOES GIVE COMPETITIVE SERVICE TO CEDAR RAPIDS. THEIR PRESENT RATE IS 24¢ WHILE NEARBY COMPETITION SITUATED ON THE OTHER LINE CAN GO TO CEDAR RAPIDS FOR 11¢. MOREOVER, ONE OF THE ELEVATORS SPECIALIZES IN MERCHANDISING WAXY CORN FOR AREA FARMERS BUT ARE FORCED TO RELY ON AN EASTERN MARKET WHILE A LUCRATIVE WEST COAST MARKET IS NOT AVAILABLE FOR BASICALLY THE SAME REASONS STATED. IT IS SITUATIONS LIKE THIS THAT MUST BE CORRECTED AS WELL AS THOSE EXISTING AT GATEWAY OR INTERCHANGE POINTS WHICH ALLOW UNCONTESTED CANCELLATION OF JOINT RATES AND/OR RECIPROCAL SWITCHING.

I'M SURE YOU ARE AWARE THAT IN MANY CASES THE SWITCHING CHARGE HAS BEEN TAKEN OUT OF THE LINE-HAUL RATE AND PLACED IN A SEPARATE TARIFF AT AN EXORBITANTLY HIGH RATE WHICH MOST EFFECTIVELY CANCELS THE RATE AS WELL.

I WOULD BE REMISS IF I DID NOT VENTURE FOR A MOMENT INTO ANOTHER AREA OF STAGGERS THAT IS AGAIN, FOR ALL PRACTICABLE PURPOSES, WITHOUT REMEDY FOR MOST COUNTRY ELEVATORS. THIS IS CONTRACTING WHICH IS BECOMING MORE PREVALENT IN THE GRAIN INDUSTRY BUT DUE TO DISCLOSURE RULES OF THE COMMISSION FORCES A COUNTRY ELEVATOR TO SUBSCRIBE TO A CONTRACT REPORTING SERVICE TO EVEN KNOW WHEN HE IS BEING UNDERCUT BEFORE IT IS TOO LATE. THE USUAL SITUATION IS THAT THE SMALLER COUNTRY ELEVATORS ARE NOT EVEN AWARE OF A COMPETITIVE SITUATION CREATED BY CONTRACT UNTIL IT IS PRACTICALLY TOO LATE TO DO ANYTHING ABOUT IT. WITH THE COMMISSION NOW AUTOMATICALLY GRANTING AN IMMEDIATE EFFECTIVE DATE THIS FURTHER EMASCULATES THE INTENT OF STAGGERS WHICH WAS FIRST UNDERSTOOD TO GRANT A 30 DAY EFFECTIVE DATE PERIOD. WHEN A SHIPPER DOES BECOME AWARE THAT MOST OF HIS BUSINESS IS GOING CROSS COUNTRY HE THEN HAS TO INITIATE AN ACTION WITHIN THAT 30 DAY PERIOD AND FILE A COMPLAINT, WHICH INCLUDES REQUESTING DISCOVERY OF SECOND TIER CONTRACT TERMS. IF HE IS SUCCESSFUL IN PROVING UNREASONABLE DISCRIMINATION HE MAY FIND THAT A SIMILAR CONTRACT HE NOW HAS THE RIGHT TO HAS BEEN "FILLED" BY A PARTICULAR AGREEMENT OR CONTRACT ENTERED INTO BY HIS COMPETITOR AND AN INDIVIDUAL

PROCESSOR OR TERMINAL POINT. HE IS THUS LEFT IN THE UNENVIABLE POSITION OF EITHER HAVING HIS ORIGINAL GRAIN MERCHANDISING AREA DEPLETED OR UNABLE TO SHIP TO THE DESTINATION DUE TO THE DESTINATION BEING A CO-CONTRACTOR WITH HIS LOCAL COMPETITION. IN FINALITY, HOWEVER, THE LEGAL AND TRAFFIC MANAGEMENT EXPERTISE NEEDED TO LITIGATE AN ALLEGED DISCRIMINATORY CONTRACT SITUATION IS BEYOND THE FINANCIAL RESOURCES OF MOST GRAIN SHIPPERS.

IN CONCLUSION, PERHAPS S.477 IS THE APPROPRIATE VEHICLE TO ENFORCE, ON REASONABLE TERMS, A CARRIER TO CONNECT WITH TRACK OF A COMPETING CARRIER OR TO REACH THE SHIPMENT DESTINATION, BUT THERE ARE DOUBTS RAISED AS TO WHETHER OR NOT THE ANTI-TRUST ACTS ARE THE VEHICLE TO USE.

LET ME NOW CLOSE BY QUOTING A PASSAGE FROM A FAVORITE ACT OF MINE:

"It shall be the duty of every common carrier subject to this part to provide and furnish transportation upon reasonable request therefor, and to establish reasonable through routes with other such carriers, and just and reasonable rates, fares, charges, and classification applicable thereto; and it shall be the duty of common carriers by railroad subject to this part to establish reasonable through routes with commommon carriers by water......and in case of joint rates, fares, or charges, to establish just, reasonable, and equitable divisions thereof, which shall not unduly prefer or prejudice any of such participating carriers."

Not a bad requirement - in fact a very good one.

Thank you.

Senator GRASSLEY. OK. Thank you. You're next. You didn't think you and I would get together so soon, did you?

STATEMENT OF RICHARD L. CROM

Mr. CROM. No. I missed you last Friday night. I am the president of Walnut Grove Products, and we're in the feed business. We have five feed plants in Iowa, one in Wisconsin, and one in Nebraska. We employ 400 people in the State of Iowa.

W.R. Grace is a diversified company and is involved in meat packaging. Their Cryovac Division is in Cedar Rapids, which produces film. This activity supports the innovation of boxed beef. In addition, the company is involved in the fertilizer business in Iowa and, in total, W.R. Grace employs about 1,000 people in the State.

I'd like to comment a minute here that we do appreciate the work you've been doing on behalf of agriculture, and your leadership last fall helped bring about some activities that I think helped rural Iowa.

Second, we're also in favor of your work with the Defense Department and your proposed freeze on expenditures. So much for that. I do think Iowa is being well represented.

This hearing on S. 447, the Railroad Antimonopoly Act of 1985, is real important, as far as we're concerned. In the feed business, we need a more efficient industry, in terms of a more competitive railway system. In our feed business, we can only use railroads on incoming wheat midds, which is a flour milling byproduct. This is due to the fact that in most other situations, trucks offer lower costs and better service. Even when rail is used for delivery of midds, the service is very erratic. We must set aside inventory space for this product because we cannot predict its arrival time. Thus, we carry 200 percent more inventory of midds than is needed. Much of the delivery of midds is a simple haul from Minneapolis to either Des Moines, Independence, Monticello, Wisconsin, or Cherokee, IA, as far as we're concerned.

One point I would like to make, and that is why are we in favor of bill 447: What does it do for Walnut Grove?

No. 1, we feel this bill could enable carriers to come in and compete for business, offer more dependable, timely service, and a lower cost. In turn, with our costs lower, we would pass on the savings to farmer feeders in order to remain competitive with other feed companies, feed suppliers. As it is now, we often pay a premium for truck deliveries in order to receive dependable service.

We would like to use rail service for incoming soybean meal, which is our largest volume ingredient, and also phosphates. But since we use "just in time" inventories and because railroads are not dependable on tight scheduling, it is impossible. Of course, much of our transportation needs are in the short-haul situations. In those cases, rail is not competitive with trucks. I think this could be changed by some effort on the part of railroad management.

It doesn't make sense to me for a truck, with one driver, and hauling 20 tons of product down the highway, to be competing with a train crew who could haul 100 cars, with each boxcar holding 40 to 60 tons. Our highway repair bill could be reduced drastically if our railroads were used more extensively. We are, however, making some headway with recent developments of hopper car grain trains.

The passage of Senate bill 447 does not imply a competitive advantage in our feed business. Our chief competitors are the cooperatives: Land-O-Lakes, Growmark, and Farmland. Also competing are Purina, Allied Mills, Cargill, and Kent. Bill 447 will provide lower costs for each of us in the long haul. This will result in lower feed costs for our farmer-feeders, since transportation will realize the benefit of greater competition. Movement of ingredients and finished feeds to a farm is 30 to 40 percent of our total feed costs. A little savings on big items such as this is highly significant.

Bill 447 is important to other Grace activities in fertilizer and coal. We need rate relief in captive shipping situations, and we certainly would be pleased to have your support of this legislation to correct existing problems. Thank you.

Senator **Grassley**. Mr. Crane?

STATEMENT OF DONALD A CRANE

Mr. **Crane**. It is a pleasure to be here, sir. The other day, when I was getting ready, I heard the lyrics of a song that I thought was written about captive shippers: "Slim to none are your chances of winning." Then a little closer, I found out it was about the Iowa lottery. And I think that that's probably the way captive shippers feel when they sit down and try to deal with a railroad: slim to none.

Senator GRASSLEY. That's referred to as a "lootery" in Iowa.

Mr. CRANE. A "lootery." Well, we'll leave that one.

The economic revitalization and deregulation of the railroads over the last few years raises the basic question of what is the role of competition in the industry. What does economic freedom for the railroads mean? And do the same checks and balances that apply to other businesses apply to railroads?

The basic strength of our economic system and the common element in the answer to each of the questions is allowing competition to set reasonable prices.

S. 447 is designed to provide the benefits of competition to shippers captive to a single railroad for its central facilities. This legislation substitutes marketplace forces for an enhanced regulatory presence. And as you know, a prime indicator of vigorous competition within an industry is the full application of the antitrust laws.

In addition, S. 447 will increase efficiency in government. It will strengthen the rail industry. It will inject new factors into decisions on abandonments, and offers the potential for increasing railroad employment.

I would also like to add at this point that the bill reinstates injunctive relief for a person who is aggrieved, and the injunctive relief under the provisions of the Sherman Act, if something has to be sought and decided in 30 days, is a document clearing and it's an immediate first step in a process which is unavailable to people now. There is a shield. You can't seek injunctive relief against the railroads, and I would say that it would provide a very early quick indicator, of not unreasonable expense, to avoid the delays which even have been identified with the ICC-type proceedings by Mr. Perkins, Mr. Ludlow, and a few others.

Senator GRASSLEY. You're taking a little different approach than the last panel or Commissioner Varley did; that the antitrust laws are too slow to accomplish any good. What you just said would be an indication that they can be speedy if adequate use is made of them.

Mr. CRANE. I think that the answer to your question is yes, sir. Now, I'm not suggesting if you have one or two major cases, like *MCI* v. *AT&T,* that these get done in 30 days, or even necessarily 2 years. But you don't have, in terms of fixed telephone lines now or fixed lines in the ground use as a carrier, the Gray Telephone Co. or other telephone companies aren't taking the position that AT&T did many years ago, so you have maybe some landmark cases which will take a little effort, but that will set the pattern for a very speedy type of resolution between other parties in the private sector.

The second important ingredient that is in S. 447, which is changed, is the fact that the Clayton sanctions, triple damages would apply if the act were enacted. What this does is create a penalty if the monopolist loses. At the present time, under the Staggers and the Interstate Commerce Commission Acts, there is no financial penalty for a railroad posting, moving ahead. And if years later the ICC says, "Oh, the rate was too high", all they do at that point is adjust the rate. And so, the burden is continually on the petitioner. And so, I would suggest that the combination of injunctive relief and the sanctions substantially change both the attitude of which and the exception of which parties would sit down and negotiate, as well as the potential speed of settlement, once indicators are there. Injunctive relief granted, there would be a greater—obviously, with the sanctions there—a greater tendency on the part of railroads to try to come to terms with the shipper.

Senator GRASSLEY. You see it as a shotgun behind the door——

Mr. CRANE. Well, it certainly——

Senator GRASSLEY. To change behavior if that potential were out there—the antitrust action?

Mr. CRANE. Yes, sir.

Senator GRASSLEY. Table damage and injunctive relief?

Mr. CRANE. Yes, sir.

Senator GRASSLEY. That would not necessitate, then, in actual practice, the long, drawn-out affairs by the court approach, that would then nullify any beneficial impact of the antitrust act applicability as compared to the reregulation of the commerce bill?

Mr. CRANE. That is correct, sir.

Senator GRASSLEY. OK.

Mr. CRANE. The third point I'd like to make is that competition does work. Early this year, the Chicago North Western gained access to several mines in the Powder Basin over lines that the Burlington Northern owns and hauls, and that which they were the sole provider of service before. The coal in question was coal going down to Austin, and as soon as the CNW gained access, coal rates dropped 30 percent to the Austin utility. The Chicago North Western, with that access to those three mines, has been aggressively marketing, and I understand recently there's some contracts have been signed in Wisconsin, which again represented a substantial reduction over the sole facility, line and cost.

So I think we have, on that hand, a very recent and a very dramatic example of the potential of competition with respect to the bulk movements. These examples and other issues are addressed in the full statement.

[The prepared statement follows:]

GRACE

TESTIMONY BEFORE THE

COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON ADMINISTRATIVE PRACTICE AND PROCEDURE

U. S. SENATE

In Support of

THE RAILROAD ANTIMONOPOLY ACT OF 1985

S.447

August 29, 1985

Waterloo, Iowa

Donald A. Crane
Consultant
W. R. Grace & Co.
3333 Quebec Street, Suite 8800
Denver, Colorado 80207
(303) 399-0779

Good afternoon. I am Donald A. Crane, a consultant to W. R. Grace & Co., and I am here today appearing on behalf of GRACE in support of S.447.

GRACE has a vital interest in a healthy, vigorous and competitive railroad industry.

GRACE produces and ships many bulk commodities: phosphate from Florida to the midwest; vermiculite from Montana and South Carolina to our construction products plants in Massachusetts; coal from northwest Colorado to other points in Colorado and Texas; and bulk chemicals from coast ports and facilities to many inland destinations.

These commodities, are for the most part, tied solely to railroads for transportation. Trucks, vessels, barges and pipelines are often not viable competitive modes for these products. It is this obligational relationship that makes us 'captive' to railroad transportation and is subject to the exercise of abusive use of monopoly power when only one railroad is available for transport.

In a historical perspective, one of the functions of a highly regulated environment was to assure that monopoly powers of the railroads were kept in check, and in return, the railroads, by virtue of their complete regulation under the ICC, were shielded from prosecution under the antitrust acts. The roots of the ICC were to protect the railroads from each other's monopolistic practices and the consumer benefitted in many instances. The ICC was not set up as a consumer protection agency.

The prescience that the ICC would be a protector of railroad interests was stated near the turn of the century. I quote from a speech given in 1956 by Leland Olds, an early Chairman of the Federal Power Commission:

> "This reminds me of a letter written more than sixty years ago by Richard Olney, subsequently Attorney General under President Cleveland, to President Perkins of the Chicago, Burlington & Quincy Railroad. Perkins was disturbed lest the newly-established Interstate Commerce Commission cause trouble for the railroads. He wrote Olney asking his advice on how to bring about the elimination of the Commission.

> In order to evaluate the bids over the 1985 - 1990 time period in which coal would be delivered, it was necessary to forecast estimated freight rates through 1990. The history on the current movement to Neal #3 from Hanna, Wyoming on the Union Pacific/Chicago and North Western railroads (UP/C&NW), and the current movement to Neal #4 from Gillette, Wyoming on the Burlington Northern/Chicago & North Western (BN/C&NW), provided a basis for future escalation on the present UP/C&NW movement from Hanna and the proposed movement on the D&RG/UP/C&NW out of Hayden Gulch. It's common knowledge in the railroad industry that the D&RG rate quotations are equal to or higher than those presently being made by the Burlington Northern Railroad. I therefore used the Bulington Northern escalation as one basis for escalating the D&RG rate. For the period 1979 through 1981 the UP rate escalated at an average of 15.6% per year. The BN rate escalated at an average of 21.5% per year. Because of the large discrepancy, I decided to use an average of the UP/BN rate to escalate the D&RG Tariff. The average was 18.55%." (emphasis added) From affidavit of D. F. Stoll, Manager, Fuel Supply, in Docket No. WRU-82-12-154, September 22, 1982.

GRACE, like Iowans, is deeply concerned about the captive transportation disadvantage due to the exercise of unrestrained railroad monopoly power.

These unregulated monopoly railrates cut both ways: they permit damage to producers and gouging of the consumers!

APPROACH: COMPETITION OR REGULATION?

There are two general approaches to solving the plight of the captive shipper: reregulation under the ICC or the creation of a business environment that would assure competitive rail rates in those instances of service by only one carrier.

Grace believes the best approach is to inject the potential for competitive rail service into captive shipper situations. This is accomplished by making trackage rights available to captive shippers under the provision of the

Sherman-Clayton Acts. This approach uses the free enterprise mechanism of competition to arrive at a fair price for service rather than the heavy regulatory hand of a bureaucracy.

What are Trackage Rights?

Trackage rights is the common railroad term used to describe the ability for trains of one railroad to use the tracks and terminals of another railroad under reasonable terms (including compensation). Trackage rights are commonly accepted by the railroads in circumstances limited to: a) movement at terminal facilities; b) voluntary trunk line movements between two railroads; and c) the provision of trunk line movements to a third carrier as a condition of rail mergers between other carriers. Trackage rights can cover any distance, for instance the D&RGW has such rights for nearly 1,000 miles from Denver to Kansas City. The viability of some railroads depends entirely on such rights, for instance the Utah Railway and the Missouri Kansas City Southern.

What is the Plight of Captive Shippers?

At the present time, a captive shipper has virtually no ability to bargain with the sole facility railroad. The shipper must accept the freight rate offered for all practical purposes, or not make the shipment. While this condition has always existed, historically the ICC regulated every tariff and the freight rates established included consideration of other regulatory objectives. ICC regulation of tariffs led to the creation of the condition of 'differential' or 'discriminatory pricing'. This is the imposition of a disproportionately high rate for the freight movements that are obligated to railroads in order to assure sufficient revenues to cover the other rail services required by the pervasive regulatory system.

However, with the passage of the Railroad Revitalization and Regulatory Reform Act in 1976, and the Staggers Act in 1980, the presence and authority of the ICC was substantially curtailed. These Acts also substantially abolished most of the various societal objectives with respect to service that required the pervasive regulatory presence.

How Does Trackage Rights Help?

If captive shippers had the ability to exercise trackage rights from the producing facility to the point where competitive rail service is available for the shipment, then freight rates over the sole facility, and therefore the remainder of the haul, would approximate that of competitive service. The sole facility carrier would agree to a competitive rate or lose the haulage to a competitor who would provide the service.

The existence of trackage rights, for captive shippers to exercise, assures the competitive negotiating framework upon which our free enterprise system operates. A competitive framework is necessary in the absence of pervasive regulation.

In all practicality, it is likely that sole facility carriers would choose to provide the service at a competitive rate. Thus, the actual exercise of trackage rights would be infrequent at most.

How Would Trackage Rights Work?

Under S.447, trackage rights can be exercised only if the sole facility carrier insists on a monopolistic freight rate for the use of its facilities and denies access to its tracks by a competitor. If the sole facility carrier matches or comes reasonably close to any competitive offer (or a pro-forma evaluation of the cost of providing the service by the shipper), then the sole facility owner provides the service.

A captive shipper would solicit bids from several railroads, including the sole facility owner. The competing railroads, based on their own experience, would have a basis to judge what a reasonable charge would be for the use of the tracks of the sole facility carrier. The shipper would then negotiate with the bidders to arrive at the lowest possible rate and then if that was not matched by the sole facility railroad, determine if the spread was sufficient to trigger the exercise of the trackage rights.

If trackage rights were exercised, then the practical aspects of the joint use of tracks and facilities that apply to current trackage situations would be controlling. Obviously, the competing railroad would have adequately licensed and qualified engineers, trained crewmen and the like. Similarly, an affirmative obligation for the appropriate equipment and its adquate maintenance would exist for the carrier performing the service. Again, operational and safety considerations for the joint use of tracks or terminals by two or more carriers are satisfactorily resolved on an ongoing basis under current railroad practices.

Competition and Railrates

Of more than passing interest is the experience of coal shippers. Where competitive rail service is available (say from the Colorado Front Range to Texas) coal freight rates average about 1.5 cents per ton mile. Where competitive rates are not available, coal freight rates range up to 11 cents per ton mile and do not match competitive rates. Similarly, the introduction of competition in rail service to mines in the southern Powder River Basin resulted in coal haulage rates dropping by 30% to destinations in Texas. Coal shippers readily concede that the availability of rail competition substantially reduces haulage costs.

OTHER ASPECTS OF THE COMPETITIVE APPROACH

Costs of Reregulation/Efficiency of Government

The alternative to the free-enterprise approach of injecting the potential for competition into captive situations is to reregulate the railroads.

Reregulation necessary to implement Congressional concern for protecting captive shippers can only lead to a larger pervasive regulatory bureaucracy, the dilemma that Congress faced in the first instance.

In addition, reregulation will prove costly to captive shippers. On the one hand they will bear the costs of preparing pleadings and assuring representation before the ICC. On the other hand, it is likely that the Administration will seek to recover costs of such special and enhanced regulation through administrative fees placed on captive shippers that avail themselves of the ICC.

These costs of reregulation can be avoided and eliminated by creating the basis for competition for captive rail service by passing S.447.

Abandonment of Tracks

Presently, any owner of abandoned track is entirely dependent upon the connecting carrier, who abandoned the track in the first instance, for service. However, under S.447, the owner or operator of "abandoned" track would have the ability to exercise the competitive provisions and thus be able to assure rail service for shippers on that line. S.447 puts a premium on continued use of branch lines. In short, S.447 increases the value of railroad rights-of-way, and this benefits rural America.

Railroad Employment

From 1980 to 1983, employment in Class I railroads decreased by 30% from 480,410 to 341,507. Employment in the industry is still contracting at a rate of 14% per year while traffic overall is increasing modestly at over 3.8% per year. The continuing decrease in employment is heralded by some, under the guise of efficiency, as one of the benefits of railroad mergers. Two additional major mergers are pending, that of the Santa Fe and Southern Pacific and the proposed sale of Conrail to Norfolk-Southern.

We believe that S.447 will aid in the reversal of this decrease in employment. The potential for increased competition within the rail industry will make the rail option more attractive to shippers. Traffic that is now lost to other modes due to monopoly rail rates should be re-captured. Traffic that has been lost due to product competition, will be re-kindled. The sharpening of all rail transport prices through competition, along with the technological and service innovations available, will lead to increased traffic and employment in the industry. The provisions of S.447 also address many of the anticompetitive concerns inherent in rail mergers.

The Role of the Federal Courts

Critics maintain that S.447 might turn the Federal Court System into hundreds of mini ICC's.

This criticism reflects the depth of the regulatory mentality imbued in the industry; e.g. the industry's perceived need for a regulator to approve its decisions.

Under S.447, the Federal Courts will not regulate the railroads any more than they regulate other private enterprises. With the inclusion of injunctive relief (Sec. 9(d)(2)) and triple damage penalties (Sec. 9(d)(1)), the competitive provisions of S.447 are largely self-enforcing. This is one reason why the application of the Sherman-Clayton Acts is considered a primary indicator of the free enterprise system at work.

Rights of Ownership

S.447 protects the rights of ownership through the same statutory framework that protects other industry, that of the Sherman-Clayton Acts. The competitive access provisions in S.447 require reasonable compensation to track owners. Yet, S.447 provides additional protection by assuring the right of the owner/carrier to provide service at a competitive rate (Sec. 9(a)(3)). This, in effect, is a "right of first refusal" for the owner/carrier to meet "the competition". These dual safeguards assure rights of ownership within a competitive, but not monopolistic, framework.

Innovative Services

One of the significant rail innovations in the last 15 years is the creation of unit train service for shipments of coal. Unit train service was developed in response to competition from the first coal slurry pipeline in eastern Ohio. As unit train service was extended to other coal areas, it led to further improvements in loading and unloading facilities in order to reduce costs and maintain markets.

Just as the unit train concept was developed and perfected to meet certain needs of the coal and utility industry, new challenges are on the horizon for railroads.

The approaches to rail management on how to operate innovative services safely and profitably, are enhanced by the provisions of S.447. The management practices, fostered by the competitive provisions of The Railroad Antimonopoly Act, are those which will be required to meet these coming challenges.

SUMMARY

The potential competitive access provided for in S.447 is the free enterprise alternative for resolving the dilemma of captive rail shippers. It uses the competitive framework of our economic system as a substitute for pervasive governmental regulation, yet its terms of use and provisions for compensation are not a challenge to private property ownership and rights.

Senator GRASSLEY. Thank you. Mr. Voss?

STATEMENT OF TERRY J. VOSS

Mr. Voss. Thank you, Senator. I'll highlight my speech, and the balance of it is in the prepared statement you have.

I am president of the United Purchasers Association in Des Moines, which is owned by seven cooperatives throughout the State. We have 39 grain facilities located in Iowa. UPA is also a member of an unincorporated association called Shippers Committee, OT-5, or SCOT-5, of which I serve as president of that group, whose 32 members include large and small grain companies, not only in Iowa, but throughout the country. AGRI-Industries, a regional cooperative headquartered in Des Moines, with upward of 300 cooperative members, is also a member of SCOT-5, and they support this statement today, also.

The name "Shippers Committee, OT-5" reflects a regulation of the Association of American Railroads, labeled as circular OT-5, which, in tariff form, is used by the railroad industry to control, limit or veto the supply and use of private covered hopper cars by shippers. The grain industry has been extremely concerned about that policy for a number of years because it is a policy which threatens not only the investments that may of us have been forced to make in covered hopper cars, but also the ability of grain originators to market their products during those times when railroad cars are in short supply, as they have been for many years in the not-too-distant past, and as they may again be in the future.

As the production of grain exports soared to the new heights in the mid and late 1970's and the early part of this decade, which has largely been sustained from a volume point of view, the railroads were actually reducing their grain-carrying capacity. For example, during the 1970's, we experienced shortages of as much as 30,000 grain-type railroad covered hopper cars per day. Grain literally rotted on the ground for lack of transport. And grain producers, such as those here in Iowa, who are located long distances from their markets, and who thus rely heavily on rail service to reach those markets, lost untold millions of dollars in both deteriorated product and sales opportunities.

Beause the railroads proved themselves unwilling or unable to supply an adequate number of grain-type covered hopper cars, shippers were impelled to do so themselves. Through a number of devices that I won't take your time to describe now, the railroads actually encouraged, and in some cases coerced, us to do so. The Interstate Commerce Commission itself sent its officials here to Iowa and around the Nation, giving speeches that urged grain shippers to supply their own covered hopper cars.

Responding to those pressures, grain shippers began to acquire large fleets of covered hopper cars. Whereas in 1973, shippers supplied 9,700 of the grain-type covered hopper cars, by 1982 they supplied 75,000, or 44 percent, of all such cars in use on the railroads.

A few years ago, however, the railroads began to experience surpluses of grain-type covered hopper cars. Since these surpluses developed, railroads have taken the position that they are entitled to exercise their authority to cause shipper cars to be idled and, thus, to force shippers who find it necessary to ship grain by rail to do so in cars which the carriers own or furnish. To put it another way, the railroads began using their substantial economic power to tell us that they may, if they wish, force us to use cars which they supply as a condition to our use of their other facilities.

Let me assure you there is nothing unique about a grain-type covered hopper car. The cars which we shippers acquired and still, to a large extent, operate, are no different than the cars which the railroads operate. Our cars meet mechanical and safety specifications set by the railroad industry, just as their own cars do, so there is no quality control reason for any railroad to insist that its cars be used in preference to ours. What is involved is simply the fact that railroads, who still have exclusive control over their own rights-or-ways that we grain shippers must use in order to market our products, are taking advantage of that substantial economic power in order to insist that we also use their cars if they so dictate, even though we may have our own cars or access to cars available on the open market.

S. 447 addresses situations in which railroads use their exclusive control over track and other facilities to engage in monopolistic practices. The overwhelming number of grain elevators are served by only a single railroad. As the Senator no doubt knows, the storage facilities of these elevators, which are sorely needed in these times of bumper harvests, are used primarily for crops that eventually will reach distant markets. Once grain comes to a country elevator, it is, therefore, fairly well committed to the stream which moves grain to market.

Most markets for grain in country elevator storage are distant markets. In the case of Iowa, for example, much of our grain moves to the Pacific Northwest for export, while significant quantities also move to feedlots in California, Arkansas, and Texas. Railroads play an essential and, in many cases, irreplaceable role in these movements. For country elevators served by a single railroad and needing to reach these markets, there is indeed a true railroad monopoly.

We are not in support of the reregulation of the railroad industry. However, we do not believe that railroads should use that monopoly power to condition the use of essential railroad facilities supplied exclusively by the railroads—their right-of-way and their locomotive power—upon the use of other facilities—namely, private covered hopper cars—which are available from alternative sources of supply for use on terms more advantageous than those which apply when railroads insist that we use their cars.

Language in Senate 447 would make it unlawful for carriers to condition the use of the sole railroad facility upon the use of other facilities of the rail carrier. I am here today, on behalf of UPA and SCOT-5, to urge the Senator and other members of this Committee on the Judiciary to give favorable consideration to such language for the purpose of prohibiting monopolistic activity by railroads in the control of the freight car supply and use. Thank you.

[The prepared statement follows:]

STATEMENT OF TERRY J. VOSS
BEFORE THE
HON. CHARLES E. GRASSLEY
UNITED STATES SENATE, COMMITTEE ON THE JUDICIARY, AT WATERLOO, IOWA
AUGUST 29, 1985
CONCERNING S. 447, THE RAILROAD ANTIMONOPOLY ACT OF 1985

Senator Grassley and Members of the Committee Staff:

My name is Terry J. Voss. I am President of United Purchasers Association of Des Moines, Iowa, and I am very pleased to have this opportunity to meet with you today here in Waterloo. UPA is owned by seven co-ops which operate a total of 39 grain facilities in Iowa at locations shown on the attachment to my statement.

UPA is a member of an unincorporated association called Shippers Committee, OT-5, or "SCOT-5," and I serve as President of that group, whose 32 members include large and small grain companies not only in Iowa, but throughout the country. Agri Industries, a regional co-op headquartered in Des Moines, with upwards of 300 co-op owners, also is a member of SCOT-5.

The name, "Shippers Committee, OT-5," reflects a regulation of the Association of American Railroads, labelled as Circular OT-5, which, in tariff form, is used by the railroad industry to control, limit, or veto the supply and use of private covered hopper cars by shippers. The grain industry has been extremely concerned about that policy for a number of years because it is a policy which threatens not only the investments that many of us have been forced to make in covered hopper cars, but also the ability of grain originators to market their products during those times when railroad cars are in short supply, as they have been for many years in the not too distant past, and as they may again be in the future.

I am sure that the Senator recalls the recurring problems faced by Iowa grain producers and others in attempting to get their products to a competitive marketplace, only to be stymied by recurring shortages of railroad cars during the 1970s and the beginning of this decade. The fact of the matter is that, as grain production and grain exports soared to new heights in the mid and late 1970s and the early part of this decade -- which largely have been sustained from a volume point of view -- the railroads were actually reducing their grain-carrying capacity. During the 1970s, we experienced shortages of as much as 30,000 grain-type railroad covered hopper cars per day. Grain literally rotted on the ground for lack of transport, and grain producers, such as those here in Iowa, who are located long distances from their markets, and who thus rely heavily on rail service to reach those markets, lost untold millions of dollars in both deteriorated product and sales opportunities.

Because the railroads proved themselves unwilling or unable to supply an adequate number of grain-type covered hopper cars, shippers were impelled to do so themselves. Through a number of devices that I won't take your time to describe now, the railroads actually encouraged, and in some cases coerced, us to do so. The Interstate Commerce Commission itself sent its officials here to Iowa and around the nation giving speeches that urged grain shippers to supply their own covered hopper cars and repeated that advice in private meetings, such as some which I, personally, attended.

Responding to those pressures, grain shippers began to acquire large fleets of covered hopper cars. Whereas in 1973, shippers supplied 9,777 of the grain-type covered hopper cars, by 1982 they supplied 75,542, or 44 percent of all such cars in use on the railroads.

A few years ago, however, the railroads began to experience surpluses of grain-type covered hopper cars, in part as a result of the prior Administration's grain embargo, and those surpluses have been fairly constant ever since, although they continue to be marred by periodic, regional shortages. Since these surpluses developed, railroads have taken the position that they are entitled to exercise their "OT-5" authority to cause shipper cars to be idled and thus to force shippers who find it necessary to ship grain by rail to do so in cars which the carriers own or furnish. To put it another way, the railroads began using their substantial economic power to tell us that they may, if they wish, force us to use cars which they supply as a condition to our use of their other facilities.

Let me assure the Senator that there is nothing unique about a grain-type covered hopper car. The cars which we shippers acquired, and still, to a large extent operate, are no different than the cars which the railroads operate. Our cars meet mechanical and safety specifications set by the railroad industry, just as their own cars do. So there is no quality control reason for any railroad to insist that its cars be used in preference to ours. What is involved is simply the fact that the railroads, who have exclusive control over their own rights-of-way that we grain shippers must use in order to market our products, are taking advantage of that substantial economic power in order to insist that we also use their cars if they so dictate, even though we may have our own cars or access to other cars available on the open market.

Railroads today find comfort for their position in certain decisions of the Interstate Commerce Commission which, the railroads claim, give them the right to exclude or limit private cars at will. Although SCOT-5 is challenging those claims in litigation pending before the Commission, just as other shippers have attempted to obtain other forms of competitive access in I.C.C. litigation, we feel strongly that legislation is needed which plainly would make this type of monopolistic behavior subject to recourse under the antitrust laws.

S. 447 addresses situations in which railroads use their exclusive control over track and other facilities to engage in monopolistic practices. The overwhelming number of grain elevators are served by only a single railroad. As the Senator no doubt knows, the storage facilities of those elevators, which are sorely needed in these times of bumper harvests, are used primarily for crops that eventually will reach distant markets. Once grain comes to a country elevator, it is, therefore, fairly well committed to the stream which moves grain to market.

Most markets for grain in country elevator storage are distant markets. In the case of Iowa, for example, much of our grain moves to the Pacific Northwest for export, while significant quantities also move to feedlots in California, Arkansas, and Texas. Railroads play an essential, and in many cases irreplaceable, role in these movements. For country elevators served by a single railroad and needing to reach these distant markets, there is indeed a true railroad monopoly.

SCOT-5 does not believe that railroads should use that monopoly power to condition the use of essential railroad facilities, supplied exclusively by the railroads — their right-of-way and their locomotive power — upon the use of other facilities -- namely covered hopper cars — which are available from alternative sources of supply for use on terms more advantageous than those which apply when railroads insist that we use their cars.

Language in S. 447 would make it unlawful for rail carriers "to condition the use of the sole railroad facility upon use of other facilities" of the rail carrier. I am here today on behalf of UPA and SCOT-5 to urge the Senator and other members of the Committee on the Judiciary to give favorable consideration to such language for the purpose of prohibiting monopolistic activities by railroads in the control of freight car supply and use.

Thank you for your attention.

LOCATIONS OF IOWA FACILITIES OPERATED BY OWNERS OF UNITED PURCHASERS ASSOCIATION

Albert City
Hartley
Corning
Rinard
Gowrie
Ulmer
Harlan
Manilla
Marne
Ralston
Jordan
Rockwell
Bayard
Varina
Creston
Farnhamville
Slifer
Churdan
Lake City
Denison
Persia
West Phalia
Jefferson
Halbur
Dougherty
Coon Rapids
Rembrandt
Benton
Somers
Lohrville
Lytton
Yetter
Oakland
Shelby
Definance
Boone
Templeton
Yale
Herndon

Senator GRASSLEY. Unlike Chairman Varley and the panel of utilities, it appears that this panel has invited congressional action. They really would prefer to have regulatory action by the ICC, but didn't think it would come.

Considering legislative action, they probably preferred the antitrust laws to be too long in accomplishing the goals that we seek to accomplish; and you folks tend more toward S. 447. At least, I think I read that clearly from at least four of you. Maybe Mr. Ludlow was the only one who was a little hesitant to go quite that far. Is that fair to assume?

Mr. STONE. Yes, sir.

Mr. CROM. Yes, sir.

Senator GRASSLEY. And that means a preference to S. 447, as opposed to S. 477?

Mr. VOSS. The reregulation?

Senator GRASSLEY. Yes. So does that mean that you think S. 447 ought to be the exclusive approach to S. 477?

Mr. STONE. Senator, I don't believe that either one of the bills, in and of themselves, will really solve all the problems.

Mr. VOSS. I agree with Bob.

Senator GRASSLEY. That's a very necessary clarification.

Mr. CROM. I think one thing we're interested in is making sure the railroads aren't shielded by legislation which the rest of us in industry have to face day in and day out.

Mr. VOSS. Senator, I think the vehicle is in place, in essence, with the Commission. The shipper today does't really have a lot of chance in front of the Commission, unless a short trial before the hanging.

Senator GRASSLEY. Are you speaking about small organizations and small businesses? Big utilities?

Mr. VOSS. National Grain and Feed, the fertilizer industry; don't you agree, Bob?

Mr. STONE. Yes.

Senator GRASSLEY. My first question is: Under the Staggers Act, do you feel if the ICC were administering the law as it was intended by Congress, you would be protected?

Mr. LUDLOW. I think the basic elements of protection are there. As I read the parts of the act, particularly the parts that we're discussing here today, it seems to me, as I made the remark before, that the Interstate Commerce Commission and the Commissioners seem to go their own way, but I agree with Mr. Voss in his remarks about where a small shipper or where a small organization stands—or even a larger organization, such as the National Grain and Feed Association. I think Mr. Crane made some excellent points about supporting this particular bill.

Perhaps we could look back at some of the proceedings before the Commission, that lasted 10 years, between the Chicago North Western, the Union Pacific, and the Rock Island. But I think you could put more teeth into the Staggers Act itself rather than antitrust. I think it's a long road compared to what could be done by the regulatory process.

Mr. CRANE. I think, from Grace's point of view, Senator, the preference is with an approach that relies more on the comparative process than the administrative process. We see this bill as one of the opportunities to really substitute private market mechanisms for governmental activities, and to the benefit of the consumer.

Mr. CROM. I'd like to add I think we're getting about all we're going to get out of the Interstate Commerce Commission. I don't think anything further that you crank in there is going to make much difference.

Senator GRASSLEY. Mr. Voss, you brought up that business about your hopper cars or about hopper cars generally. Does this bill, 447, providing antitrust coverage, give you some relief?

Mr. VOSS. Well, Senator, to go back a little bit, we've had litigation from the Commission for 2 years. The Commission ordered the railroads to negotiate an entry position with us. They're hiding this thing under antitrust laws now, through the AAR. We feel that if they are, in fact, going to restrict the use of that, it would open up an antitrust suit.

Senator GRASSLEY. Now, as I recall, my office has been involved with trying to bring that issue to a head, and evidently we haven't been successful.

Mr. VOSS. It's been pending in front of the Commission. We've got a complaint filed in front of the Commission that's a little over 2 years old that they have not responded to.

Senator **Grassley**. Mr. Stone, cost of agriculture is important. I think you made some statement about cost, but I'd like to know what you feel the cost to the individual farmer, or at least to agriculture generally, would be under the present system for captive shippers who have no recourse.

Mr. **Stone**. OK. Basically, specifically potash—a carload of potash to an Iowa farmer will cost him about $100 a ton, and you've got $50 a ton in freight on a carload of potash coming out of Canada. It is the same on phosphates.

Senator **Grassley**. But now you'd have cost anyway, so how much of that $50 would be related to lack of competition?

Mr. **Stone**. That would be really difficult to try to identify, but as Mr. Crane says, the coal had a 30-percent reduction. I don't think a 10- to 20-percent reduction, if you had adequate transportation or adequate competition, would be out of reach at all. At least, on the east side of the State and west side of the State, where you are able to get product in by barge, and of course the barge system right now is maximized. The terminal facilities are maximized, and you just can't move that much product by barge to handle the entire demand. In those cases, you've got probably a 50-percent difference between the rail rate and what you can do by competing numbers.

Senator **Grassley**. We all know the importance to a healthy rail industry, and you testified to that. But at the same time, you object to what the rail industry might consider its backbone, and that being the rates charged for high-volume, long-distance haul. How do you reconcile what might be considered the incongruity of those two points of view?

Mr. **Crane**. Well, if I can start, I believe that from the national resources group, which is coal mining in the West, their position is that if a competitive freight rate of this captive coal area in northwest Colorado, which was addressed by one of the Iowa utilities-- Denver and Rio Grande—if the freight rate out of there is competitive, and you still can't sell the coal, then that's the lumps of opening up, so to say, the coal mine in a remote, captive area.

On the other hand, what they're experiencing now is a freight rate which isn't set competitively, which isn't really reviewed in the regulatory framework, and it's a freight rate which is making the coal uncompetitive, unsalable outside of the State or even in the front range. And it's sort of a question of how much—again, getting back to one of the folks on the utility panel—how much are you going to overcharge the obligatory traffic to subsidize other activities? And that feeling of Grace and the resource group is they would like to have some competitive pressure applied to the extent of that overcharge.

Senator **Grassley**. Do any of you others have anything to add to that?

Mr. **Crom**. I'd like to add that there's a lot of opportunity, I think, for the railroad system if it's highly efficient and delivers on time and so on. For example, on our soybean meal from Sutherland, IA, over to Independence, IA, there's no reason that can't be hauled by rail. There are things that would have to be changed in the management of the railroad, but I hink this efficiency can come through increased business. And I think, as an American public, we ought to be interested in using the most efficient transportation system available. Why pay extra for trucks and highway repair when we've got a railroad system that can work? So my answer is let's give more business to the railroads.

Mr. Voss. I don't have a lot of problem with the rate structure. We've railed stuff for 10 miles and we've railed it for 2,000 miles. I don't have a big problem with the rate structure, as a rule.

Mr. Stone. Senator, I don't think we're really attacking the backbone of the railroads. What I'm fearful of is that the captive shipper, the monopolistic movement is subsidizing the predatory pricing, where the railroads have engaged in predatory pricing against intermodal competition; trucklines, barges. And they are basically subsidizing. Maybe it's kind of a lost leader there, if they're not making that much money on that barge traffic or that competitive traffic, but they are subsidizing the overall operation. I think what we're saying is that we don't think that's equitable warfare, and in which competition they wouldn't have the ability to do that. I mean, we all, in the free enterprise system, have competition that we have to deal with, and that basically tells us there's some markets we should be in and some markets we shouldn't be in, based on our ability to compete. And that's why I feel this bill could help provide some of those alternatives.

Mr. Voss. Senator, I think, hitchhiking on Bob, you can bring anticompetitive pricing before the Commission today and litigate it 5 years, and you could flat win if the Commissioner agrees with you 100 percent. It's discretionary whether they award any damages, let alone triple damages that you would get in an antitrust suit, and I think that there has to be a paper tiger that's got some teeth in it.

Senator Grassley. OK. I have no further questioning. Do any of you have closing comments or a summary?

Mr. Stone. Senator, I'd like to just reiterate a little bit. I don't believe that 447 is going to solve all of the shipper's problems, nor do I feel that 447 will. We have seen that with competition and with effective competition, it has maintained rate levels at a reasonable level. I feel that this bill is doing nothing more than putting the railroad, since the railroads are currently deregulated, it's another step toward deregulation. It's putting them in the same arena that all free enterprise businesses deal with.

I also can see it somewhat as a deterrent, as Mr. Crane alluded to a little bit. It could be a deterrent. Because you would have the injunctive relief and the triple damages, that the railroad may look a little stronger and harder at some of their anticompetitive prices. That's all.

Senator Grassley. OK. Thank you all very much. I appreciate that.

I would now call the third panel, consisting of Tom Walsh, who's director of Market Planning with Burlington Northern Railroad in Ft. Worth, TX; and Jerry Conlon, who is senior vice president of Chicago and North Western Transportation in Chicago.

Mr. Conlon. Senator, I asked a person from the AAR to join me to answer questions which I may not be able to answer; Mr. William Harsh.

Senator Grassley. He can join you on your right.

Mr. **Conlon**. I need help, Senator.

Senator **Grassley**. OK. Mr. Walsh, you're going to give your statement, and then Jerry.

Mr. **Harsh**. I'm just here as a resource.

Senator **Grassley**. Please proceed.

STATEMENT OF PANEL CONSISTING OF: THOMAS M. WALSH, DIRECTOR, MARKETING PLANNING—GRAIN, BURLINGTON NORTHERN RAILROAD; AND J.W. CONLON, SENIOR VICE PRESIDENT, CHICAGO AND NORTHWESTERN TRANSPORTATION CO.

Mr. **Walsh**. I am very grateful to Senator Grassley for the opportunity to appear before this hearing and express my views relative to the proposed legislation. Your willingness to understand all sides of the issue reinforces my confidence in our democratic system.

While my remarks are directed toward the transportation of bulk grain and grain products, much of what I have to say has relevance to other commodities. My purpose today is to point out that the legislation proposed in Senate 447 is unnecessary and will even be counterproductive.

Grain is a demand-driven industry. This is especially evident today, when the world is flush with burdensome supplies, and demand for U.S. grain has fallen appreciably in the face of subsidized foreign production and exports. This has affected farmers, farm elevators, merchandisers, exporters, processors and transportation companies. It points up the close interdependence that exists between all facets of the industry. It is not enough to produce grain; it must also be marketed and shipped for the benefits to accrue to the participants.

Grain is bought and sold in an open, competitive fashion, generally on a delivered basis which reflects the value of the grain plus the value of the transportation and other considerations. Mostly, the buyer is indifferent as to how the grain is shipped, whether it be by farm vehicle, 8-wheeled truck, rail, barge, or any intermodal combination.

Just about every elevator has competitive truck service. Many even own their trucks and barges. If the market is close by, trucks are sufficient. In this manner, the elevator can sell locally to processors and feedlots or into a river market for subsequent movement by barge to port areas. Where the markets are more distant and truck/barge is not appropriate, it is useful to have rail service. But, with the advent of unit trains, it is no longer necessary to have physical rail service at the elevator door. A small elevator can truck to one or more of the unit train loaders and take advantage of the attractive bid made possible by lower incentive priced unit trains.

The competitive alternatives of one-way trucking, backhaul trucking, truck/barge, rail/barge, direct rail and trucking to other rail carrier unit train stations provide the shipper with an array of low cost transportation alternatives. Rail carriers are fully cognizant of these competitive alternatives and do all in their economic power to make sure that the grain produced along their lines does not cross their tracks to an elevator on a competitive line or is not lost to intermodal competition. Grain is like water; it will flow to the lowest transportation cost. While transportation costs can't make a market—demand makes the market—it does determine the mode of transportation used. In the sense that competitive and economic alternatives are readily available, there are not captive shippers.

The shrinking number of transportation entities, whether truck or barge or rail, has caused some concern about continued competitiveness among carriers and between the modes. However, one must understand that while the number of carriers declined, there exists and will continue to exist a tremendous surplus of transportation capacity on the rivers, on the highways and on the rails. And surplus capacity always spells very competitive pricing and service. It is not uncommon for Burlington Northern to have the equivalent of one-fourth of our 12,500 grain covered hopper cars stored. This creates tremendous pressure to fill up that capacity and attract as much grain as possible. We know full well that capacity cannot be inventoried. If it is not used, it is simply a lost opportunity. Our objective is to earn a dominant market share through better service and better prices. That isn't monopoly; it is competitiveness in the finest sense of the word.

As far as joint routes and rates with other carriers are concerned, we plan to maintain what is in place and negotiate additional ones, provided circuity or other economics do not dictate otherwise. That is not to say that a lower cost, direct route will not carry a lower price. We feel this additional alternative is in the best interests of our customers.

The term "captive grain shipper" is an anachronism, considering the many available transportation alternatives and the heavy surplus of transportation capacity.

Now, let me give you an example of why I think Senate 447 can have negative value. In November 1982, with the help and support of Iowa DOT, the Burlington Northern entered into an agreement to operate and purchase 100 miles of abandoned Milwaukee railroad between Council Bluffs and Bayard, IA. Subsequent to abandonment, the line was operated for about 18 months by the CNW Railroad. Both the Milwaukee and the CNW found that they were residual carriers to trucks, and they terminated service. Was BN presumptuous in thinking it could make an economic success of this line? Perhaps. But I believe the critical difference was the shippers' commitment, without penalty, mind you, to achieve certain volumes by rail, and on our part, the commitment to provide equipment and service and competitive rate levels into all the markets we serve.

When the line was inoperative, these shippers were captive to truck and truck/barge. BN rail service was a welcome alternative. It is working, and we expect it will get better. However, if under legislation such as Senate 447, we have to allow another rail carrier onto this line, the economics will be diluted, and we most certainly will have to terminate this agreement.

A similar case can be made for the numerous branch lines that are barely generating enough revenue and margin for their continued operation. Shared rail business would be a serious disincentive or line maintenance for improvements or for carrier investment in equipment and facilities.

In summary, we are not in the business of alienating our shippers by poor service and noncompetitive rates. And Terry Voss made an excellent point, that he really has no problem with our rates. Competitive intramodal and intermodal alternatives compel an aggressive competitive posture on the part of rail carriers. Please, Senator, let's not fix what is not broken. Thank you.

STATEMENT OF J.W. CONLON

Mr. CONLON. Senator, thank you very much for this opportunity. I really appreciate the chance to share our thoughts on Senate bill 447, and I'll try to summarize this statement that we're filing today.

Just to be clear from the beginning, we oppose very much Senate bill 447. We think it is a dangerous precedent and a dangerous bill. This bill amends the Sherman Act to carve out special antitrust treatment where a shipper of bulk commodities, as defined in the bill, is serve by only one railroad, a unique situation in the commercial interest of this country.

The proponents say that this is not a reregulation—or at least, some of the proponents. After today's testimony, I wonder. And it is not, in effect, to affect and to change what's happened since the Straggers Act was enacted. I question that. I believe that it is a back door to reregulation. Comments that concern many issues beyond captive shipper dominance show that there is and there always will be continuing concern about whether or not the regulation or not the regulation of railroads in this country is appropriate today. I don't share that concern, but I recognize it's there. I think, though, that this bill is an attempt to bring regulation back to the railroad industry in the market dominant area. What does the bill do? I think that's an important thing.

First, the railroad is conclusively presumed to be engaged in an unlawful monopoly—conclusively presumed—and barred from asserting any of the factual and legal defenses which normally apply in antitrust cases.

Second, the railroad can only purge itself in one of two confiscatory methods. I like that word, "confiscatory," because I think it fits this bill. It must, on request, open its tracks to another railroad to use. The rental to be paid would be pursuant to a very vague standard; so vague as to ensure lengthy litigation. If that method fails to produce a railroad competitor, the owning railroad must place a ceiling on the rate it can charge the captive. It the railroad guesses wrong at any stage, it is exposed to all of the criminal and civil provisions of the antitrust laws. This is so even though, for example, the maximum rate would force the railroad to lose traffic or money.

The theory upon which the necessity of the legislation is, in our opinion, wrong on the facts, is the fact that most shippers are only served by one railroad does not by and of itself produce a monopoly. The shipper may have perfectly acceptable alternatives. The bulk commodity may be and probably is susceptible to movement by barge or truck. For example, Senate bill 447 would make fruits and vegetables shipped in piggbyback service subject to its provisions, even though trucks are predominant in that market; in fact, have 90 percent of that market.

Furthermore, there may be product—the ability of generating plants to switch from coal to oil—or geographic—coal from one region versus coal from another—competition which influences the market. The Staggers Act—the law in place; the law the Commission can now use—permits the Interstate Commerce Commission to take these factors into account. Even in normal antitrust situations, defenses of this nature are available to the defendant.

I have other factual areas where the rates have, in fact, declined since this Staggers Act in my testimony. I'd be happy to give other examples later, if it would be helpful.

The question is really this: Should we, because people are not happy with the forum that they're now taking their grievances before, put in an extraordinary law that will confiscate private property? I believe this particular legislation has the markings of a rail nationalization bill. And that assumption is either the personalities who now administer the Interstate Commerce Commission are not following the laws dictated, or the law itself does not address the problem. Since the decisions that have been rendered by the Interstate Commerce Commission support my position, obviously I'm going to say they're doing a fine job, but I think that is the question that's being asked here.

When the Staggers Act was passed, these same issues were of great concern. The hearings that went on all that summer were on questions such as agricultural pricing, branch line abandonments and market dominance. That bill, as the Senator knows, contained many, many compromises. This area was one of them. I believe the law in place does address the problem, and I recommend that in the deliberations of the Senate, that they do address that structure that the law says in the same deliberative way they did in 1980.

Just to sum up, the bill is opposed by many people other than the railroads. The railroads certainly aren't above being self-serving. I heard us characterized as a monopolistic—I wouldn't mind being a monopoly, but I would like to make more money doing it. It hasn't been too good a business lately. But it is opposed by the FTC, the DOJ, and the FRA.

The final thing I would like to turn your attention to is that this would take the jurisdiction now exercised by the Interstate Commerce Commission and give it to 5,000 district court judges. The administrative morass of interpretation of rate regulation or kind of a back-door eminent domain by 5,000 small Interstate Commerce Commissions, I would suggest, would be horrendous.

As a final thing, I will try to answer your questions. Thank you very much again for the opportunity to bring our thoughts to your attention.

[The prepared statement follows:]

STATEMENT OF
J.W. CONLON
SENIOR VICE PRESIDENT
CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY
At
WATERLOO, IOWA
August 29, 1985

SENATOR GRASSLEY, I APPRECIATE THE OPPORTUNITY TO APPEAR BEFORE YOU AND DISCUSS S. 447, A BILL TO AMEND THE SHERMAN ACT.

I AM JEROME CONLON, SENIOR VICE PRESIDENT OF THE CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY (CNW). I HAVE WITH ME MR. WILLIAM HARSH, A CONSULTANT ON DEREGULATION TO THE ASSOCIATION OF AMERICAN RAILROADS, WHO WILL ALSO BE PLEASED TO JOIN IN THE RESPONSE TO YOUR QUESTIONS.

I AM HERE TODAY TO VOICE C&NW'S OPPOSITION TO SENATE BILL 447 WHICH AMENDS THE SHERMAN ACT TO CARVE OUT SPECIAL ANTITRUST TREATMENT WHERE A SHIPPER OF "BULK COMMODITIES", AS DEFINED IN THE BILL, IS SERVED BY ONLY ONE RAILROAD.

WHILE THIS BILL DOES NOT PURPORT TO REOPEN THE STAGGERS ACT, ITS EFFECT WOULD BE A CRUSHING BLOW TO PROGRESS MADE SINCE STAGGERS PASSAGE—THE STRENGTHENING OF THE RAIL INDUSTRY SO THAT IT CAN BETTER SERVE ITS SHIPPERS AND THE BENEFITS TO SHIPPERS THROUGH THE FLEXIBILITY OF A FREE MARKET PLACE.

THERE IS NO EVIDENCE OF AN ABUSE OF THE PRICING FREEDOMS PROVIDED IN STAGGERS THAT WOULD WARRANT THE PASSAGE OF THIS ACT.

IT IS A FACT THAT SINCE THE PASSAGE OF THE STAGGERS ACT, GRAIN AND GRAIN PRODUCTS RATES TO SHIPPERS IN IOWA HAVE DECREASED BETWEEN 20 AND 40%.

IT IS A FACT THAT OVER THE LAST THREE YEARS, RAILROAD COAL RATES HAVE INCREASED IN TOTAL BY ONLY 6.6%, AS COMPARED WITH 10.8% IN CONSUMER INFLATION, 8.1% IN RAILROAD INFLATION AND 7.0% IN TOTAL RAILROAD RATES.

THE SAME IS TRUE OF OTHER SO-CALLED "BULK COMMODITIES".

THESE FACTS SHOW QUITE CONCLUSIVELY THAT MARKET FORCES DO INDEED CONSTRAIN RAIL RATES.

WHAT DOES S.B. 447 DO?

THE THEORY OF THE BILL IS THAT THE SHIPPER OF BULK COMMODITIES IS "CAPTIVE" TO THE RAILROAD AND WITHOUT ANY EFFECTIVE PROTECTION IN THE DEREGULATED ENVIRONMENT CREATED BY THE STAGGERS ACT. FOR THAT REASON, THE TREATMENT PROPOSED FOR THE RAILROAD IS HARSH AND UNPRECEDENTED.

FIRST, THE RAILROAD IS CONCLUSIVELY PRESUMED TO BE ENGAGED IN AN UNLAWFUL MONOPOLY AND IS BARRED FROM ASSERTING ANY OF THE FACTUAL AND LEGAL DEFENSES WHICH NORMALLY APPLY IN ANTITRUST CASES. SECONDLY, THE RAILROAD CAN ONLY PURGE ITSELF IN ONE OF TWO CONFISCATORY METHODS: IT MUST, ON REQUEST, OPEN ITS TRACKS TO ANOTHER RAILROAD TO USE: THE RENTAL TO BE PAID WOULD BE PURSUANT TO A STANDARD SO VAGUE AS TO ENSURE LENGTHY LITIGATION. IF THAT METHOD FAILS TO PRODUCE A RAILROAD COMPETITOR, THE OWNING RAILROAD MUST PLACE A CEILING ON THE RATE IT CAN CHARGE THE "CAPTIVE". IF THE RAILROAD GUESSES WRONG AT ANY STAGE, IT IS EXPOSED TO ALL THE CRIMINAL AND CIVIL PROVISIONS OF THE ANTITRUST LAWS. THIS IS SO EVEN THOUGH, FOR EXAMPLE, THE MAXIMUM RATE WOULD FORCE THE RAILROAD TO LOSE TRAFFIC OR MONEY.

THE C&NW BELIEVES THAT THE BILL OPERATES UNDER A FALSE PREMISE: THAT THE STAGGERS ACT AFFORDS THE SHIPPER NO EFFECTIVE REMEDY. IN FACT, THE CASE WHERE THE RAILROAD SO DOMINATES A MARKET THAT THERE IS NO EFFECTIVE COMPETITION IS SPECIFICALLY COVERED BY THE STAGGERS ACT. STAGGERS RECOGNIZES THE NEED "TO MAINTAIN REASONABLE RATES WHERE THERE IS AN ABSENCE OF EFFECTIVE COMPETITION AND WHERE RAIL RATES PROVIDE REVENUES WHICH EXCEED THE AMOUNT NECESSARY TO MAINTAIN THE RAIL SYSTEM AND TO ATTRACT CAPITAL." IN SUCH CASES, THE INTERSTATE COMMERCE COMMISSION HAS THE AUTHORITY TO STRIKE THE RATE DOWN. FURTHER, A RAILROAD WHICH ENGAGES IN PREDATORY OR MONOPOLISTIC PRICING OR PRACTICE IS ALREADY SUBJECT TO THE ANTITRUST LAWS.

THE RESULT OF THIS FALSE PREMISE IS THAT THE RAILROAD GETS THE WORST OF WORLDS: IT IS SUBJECT TO MAXIMUM RATE REGULATION AND TO SPECIAL ANTITRUST SANCTIONS DESIGNED FOR AN UNREGULATED INDUSTRY. PUT OTHERWISE, A RATE COULD BE COMPLETELY LEGAL UNDER THE STAGGERS ACT, YET THE RAILROAD WOULD BE ACTING ILLEGALLY UNDER S.447 IF IT PUT THE RATE INTO EFFECT.

THE THEORY IS ALSO WRONG ON THE FACTS. THE FACT THAT A SHIPPER IS SERVED BY ONLY ONE RAILROAD DOES NOT BY AND OF ITSELF PRODUCE A MONOPOLY. THE SHIPPER MAY HAVE PERFECTLY ACCEPTABLE ALTERNATIVES: THE BULK COMMODITY MAY BE, AND PROBABLY IS, SUSCEPTIBLE TO MOVEMENT BY BARGE OR TRUCK. FOR EXAMPLE, S. 447 WOULD MAKE FRUITS AND VEGETABLES SHIPPED IN PIGGYBACK SERVICE SUBJECT TO ITS PROVISIONS EVEN THOUGH TRUCKS ARE PREDOMINANT IN THAT MARKET. FURTHERMORE, THERE MAY BE PRODUCT (THE ABILITY OF GENERATING PLANTS TO SWITCH FROM COAL TO OIL) OR GEOGRAPHIC (COAL FROM ONE REGION VERSUS COAL FROM ANOTHER) COMPETITION WHICH INFLUENCES THE MARKET. THE STAGGERS ACT PERMITS THE ICC TO TAKE THESE FACTORS INTO ACCOUNT. EVEN IN NORMAL ANTITRUST SITUATIONS, DEFENSES OF THIS NATURE ARE AVAILABLE TO A DEFENDANT.

FINALLY, S. 447 WOULD FIX A PROCESS THAT ISN'T BROKEN. THE UTILITY INTERESTS WHICH SUPPORT S. 447 IGNORE THE BASIC FACTS:

* IN THE FOUR YEARS FOLLOWING ENACTMENT OF STAGGERS, COAL RATES INCREASED ONLY 3.4% MORE THAN RAILROAD INFLATION AND ONLY 2.1% MORE THAN THE INCREASE IN RATES FOR ALL COMMODITIES.
* IN THE LAST THREE YEARS, THE INCREASE IN COAL RATES WAS 1.5% BELOW THE INCREASE IN RAILROAD INFLATION AND 0.4% BELOW THE INCREASE IN RATES FOR ALL COMMODITIES. IN THE LAST TWO YEARS, THE RECORD IS EVEN BETTER THAN THAT.
* WHEREAS RAIL COAL RATES COULD HAVE BEEN INCREASED 18% OVER RAILROAD INFLATION IN THE FIRST THREE YEARS UNDER A SPECIAL REVENUE-ENHANCEMENT PROVISION OF STAGGERS, INCREASES ACTUALLY TAKEN UNDER THAT AUTHORITY AMOUNTED ONLY TO .46% IN 1981, 1.41% IN 1982 and 0% IN 1983.
* BETWEEN 1972 AND 1983, RAIL COAL RATES DECLINED 1.0% IN CONSTANT DOLLARS, WHEREAS THE MINE-MOUTH PRICE OF COAL INCREASED 19.8% IN CONSTANT DOLLARS.

THAT RECORD SHOWS CONCLUSIVELY THAT THE RAIL INDUSTRY SIMPLY HAS NOT ENGAGED IN ANY SYSTEMATIC ABUSE OF MARKET POWER IN THE PRICING OF RAIL SERVICE.

ADMITTEDLY, MAXIMUM RATE REGULATION IS ONE OF THE MOST IMPORTANT CONCERNS BETWEEN SHIPPERS AND RAILROADS. THERE

ARE NO SIMPLE ANSWERS TO BE HAD AT THE STROKE OF A LEGISLATIVE PEN. THERE ARE WAYS, HOWEVER, TO REACH SOLUTIONS. OVER THE LAST YEAR, FOR EXAMPLE, A NUMBER OF NEGOTIATIONS HAVE BEEN LAUNCHED TO ADDRESS OTHER LEGITIMATE SHIPPER CONCERNS ABOUT IMPLEMENTATION OF THE STAGGERS ACT. SETTLEMENTS HAVE BEEN REACHED BETWEEN THE AAR AND BROADLY BASED SHIPPER ORGANIZATIONS, SUCH AS THE NATIONAL INDUSTRIAL TRAFFIC LEAGUE, AND ARE NOW BEFORE THE COMMISSION FOR APPROVAL. RESPONSIBLE SHIPPER ORGANIZATIONS THUS HAVE RECOGNIZED THAT ADEQUATE RELIEF CAN BE FOUND IN GOOD-FAITH NEGOTIATION WITH THE RAILROADS, TO PRESERVE REASONABLE JOINT RATES AND ROUTES, WITHOUT THE NEED TO TAMPER WITH THE STAGGERS ACT OR TO RETURN TO THE DAYS OF BURDENSOME REGULATION.

IN SHORT, TO PASS S. 447 IS TO COURT DISASTER—INITIALLY FOR THE RAILROAD INDUSTRY AND ULTIMATELY FOR ITS FREIGHT CUSTOMERS.

TO PUT THIS IN PROPER PERSPECTIVE, ONE NEED ONLY TAKE A LOOK AT THE RAILROAD INDUSTRY WHICH EXISTED PRIOR TO DEREGULATION—AND THEN COMPARE IT WITH THE INDUSTRY OF TODAY.

DURING THE 1970'S, SOME 22% OF THE RAILROAD INDUSTRY WAS IN BANKRUPTCY AT ONE POINT OR ANOTHER. THAT DIRECTLY IMPACTED IOWA WITH THE BANKRUPTCY COURT LIQUIDATION OF THE ROCK ISLAND AND THE BANKRUPTCY AND PARTIAL LIQUIDATION OF THE MILWAUKEE ROAD. THE UNCERTAINTY THAT THIS TURMOIL BROUGHT SHIPPERS IN THIS STATE WAS DEVASTATING. EARNINGS FOR THE REMAINING CARRIERS WERE ANEMIC. IN NO YEAR DID EARNINGS PRODUCE A RETURN ON INVESTMENT AS HIGH AS 3%; FOR HALF THE DECADE, THE RETURN WAS UNDER 2%. NOT SINCE THE 1950'S WERE RAILROADS ABLE TO EARN AS MUCH ON INVESTMENT AS THEY HAD TO PAY OUT FOR NEW CAPITAL.

IMPROVED EARNINGS HAVE MADE IT POSSIBLE FOR RAILROADS TO VIRTUALLY ELIMINATE DEFERRED MAINTENANCE FROM MAIN LINE TRACKS THROUGHOUT THE COUNTRY. EVEN BEFORE THE RECENT RECESSION, EQUIPMENT SHORTAGES HAD BECOME A THING OF THE PAST. INDEED, TODAY RAILROADS HAVE ENOUGH AVAILABLE FREIGHT CARS AND LOCOMOTIVES TO EASILY HANDLE AN ADDITIONAL 15-TO-20% VOLUME. AND INSTEAD OF A DECLINING MARKET SHARE, RAILROADS SEE THEIR SHARE OF THE FREIGHT MARKET GRADUALLY INCREASING.

S. 447 WOULD TURN BACK THE CLOCK ON ALL OF THIS PROGRESS. C&NW AND THE SHIPPERS AND PEOPLE OF IOWA STRUGGLED THROUGH THE PAST BLEAK PERIOD AND, WITH LUCK, WERE ABLE TO TUNNEL THROUGH. DON'T PUT US BACK THERE AGAIN!

Senator **Grassley**. You said the Department of Justice and FTC are against 447. Do yo know, are they also against 477?

Mr. **Conlon**. I think it's just this approach, Senator.

Senator **Grassley**. They're against any bill I've seen, because it creates a little more work for them. That isn't meant to detract from what you've said.

Mr. **Conlon**. Oh, I understand, Senator.

Senator **Grassley**. Now, as I recall, some court back there 50, 60 years ago declared that railroads weren't subject to the Antitrust Act because of the regulation of the ICC. So now that we're in an era of deregulation, the position of the railroads is still against the application of the antitrust acts. In other words, in this deregulated era, the reason for the antitrust exception is not as great today as it was, if it even exists today, as it was under the old pre-Staggers environment; right?

Mr. **Conlon**. My opinion is that, first of all, we are in a less-than-regulatory area. I know we've allowed it because of deregulation, but having just gone through the Milwaukee Railroad fight and other areas, if this is deregulation, I have trouble recognizing it in the clothes it's wearing. I also accept your premise that, where there is the marketplace at work, there could be room for antitrust; and, in fact, it does exist. For example, prior to 1980, the railroads could collectively set their rates in concert with others. Today we don't have that. And in discussions with other parties, we have the same obligation and the same responsibilities to not get into collusive ratemaking, so there is antitrust broadening. The art is, How do you broaden the antitrust and at the same time keep the repository regulation that still exists?

I believe it has been effectively handled, especially in the rate area. This bill, though, is a wolf in sheep's clothing. I don't believe this is traditional antitrust presence at all. This is a device that, if we don't like what you're doing with your property, we're going to allow somebody to take it away from you for a to-be-determined price. To me, that is a long way from collusive ratemaking or the other traditional antitrust concerns.

Senator **Grassley**. First of all, did either one of you have anything to add to that?

Mr. **Walsh**. I perceive this to be a direct attack on our ability to do differential pricing, because we feel, if we don't have this ability to price in this fashion, we'll have to walk away from tremendous volumes of grain that we now have at a bit above margin or whatever, but below our fully allocated cost. We feel we have to have that type of pricing, and I think ultimately this thing would destroy that type of ability.

Senator **Grassley**. As a followup, could S. 447, be redrafted to your satisfaction and still solve the captive shipper's problem?

Mr. **Conlon**. I have to respond this way: I don't see how. I think it's in the wrong form. I don't think the captive shipper problem is as materially and factually substantive as it has been portrayed, but it does strike me that, to the effect that the subject is addressed—that is, regulation—and what we are really talking about is rate regulation, so I think it has a fatal blow and it's the wrong form for the remedy.

Senator **Grassley**. But your general comment——

Mr. Conlon. My general comment on 477 is that we oppose the bill. We don't think the remedy is necessary, but I would say, having a long time having to deal with regulatory areas, if you're going to address the problem and if the Congress determines that the problem is real, and we haven't borne the burden of proof to say that it is not, it would be more appropriate to address it in a regulatory form than in an antitrust form.

Senator Grassley. Do you feel the ICC is interpreting the Staggers Act as Congress intended, and what are your specific objections to the provisions of S. 477, which amends the Staggers Act, regarding the standards used by the ICC in ratemaking?

Mr. Conlon. I'm glad to brought Mr. Harsh here. I could answer the first.

Senator Grassley. Go ahead.

Mr. Conlon. I think that the Interstate Commerce Commission is interpreting the Staggers Act as Congress intended, to the extent that Congress really focused on what was going to happen. I don't think any of the Congress could really address what they thought the future would be, and I can see in instances where an interpretation would be beyond what somne people thought at the time. But on the whole, I think the Commission is doing a good job with a very different environment. It's not easy to go from 80 years, or how many, of regulation and movement into the free market. It takes adjustment and, as we've seen in the other deregulation areas such as trucks and airlines, there are regional and other areas where people do, in fact, pay a burden so that the free enterprise system is substituted for a regulated, dictated system.

I'm only cosmetically familiar with the 477, and I was asking Mr. Harsh what's in that bill, and he started to tell me, and I thought, "I'll just bring him with me."

Senator Grassley. Go ahead, sir.

Mr. Harsh. Well, the industry's opposition to the ratemaking portions of S. 477 are that it really would bring more regulation to the railroad industry than as ever existed even prior to the Staggers Act, and its direct attack on differential pricing, which is the mechanism the Staggers Act has used to help the railroads get out of the situation that Iowa is so familiar with, that we were in in the mid-1970's, when you lost a couple of railroads out here because the railroad industry was undercapitalized.

As you know, the ratemaking test of the ICC is twofold. First, as a jurisdictional test, which is, "Is the railroad market dominant?" And if the market is found to be market dominant, then there is a second test that says, "Is the rate the railroad is charging reasonable?"

Up until last month, the Commission interpreted the market dominance in essentially, as some of the witnesses have said here, an antitrust test. They looked for any form of competition that would change it from intermodal product to geographic. The railroad industry had no problem with that interpretation, but there are a lot of shippers who did. And the Senate, through some of its Members, and the shipping community certainly made their feelings known, and the Commerce Commission responded by instituting ex parte 466 just a little over a year ago today, in which they went out into the shipping conmmunity and into the railroads and said, "If there's only problems with the way we're implementing the Interstate Commerce Act, why don't you come in and lets try to work it out." And out of that, a number of agreements were reached—voluntary agreements between the industry and shippers.

One of those agreements had to do with how the ICC was going to look at market dominance. There was a compromise agreement reached between the AAR and several shippers groups, in which it was agreed that if the shipper proved that he didn't have any intramodal or intermodal competition, then the railroads would pick up the burden of proving that product and geographic competition existed. And that voluntary agreement was submitted as a suggestion to the ICC, which started ex parte 320. And just last month, the ICC implemented new rules which changed the way in which it's going to look at market dominance.

That's very direct evidence of the way, contrary to all the testimony you're heard before today, which is that the Commission is completely oblivious to the feelings of shippers or commerce. It's direct evidence that the commerce is indeed listening to the concerns that the shippers have in reaching, and certainly happy to, if the railroad industry and shippers can agree, to implement the law in a different way.

So as of today, the regulations of the ICC read differently than they did last month. And today, if a shipper can come in and prove that he can't use railroads and he can't use trucks and barges, then the railroad has to come in and show product and geographic competition. The ICC does not.

Now, that's an extreme approach and one we feel is unnecessary, since we reached a voluntary agreement with our shippers. For a compromise way of going about that, I guess we're saying that Senate 477 seems to go further away from reality than it needs to go. Your shippers have told you today numerous cases of product and geographic competitive in the very real way.

As to rate reasonableness, that is one of the most difficult issues, and I'm sure everybody appreciates that anybody can say what is a reasonable rate, but the difficulty the industry has is that he approach that Senate 477 takes would just bury the process in paperwork. If you had one individual rate that came before the Commerce Commission on, say, coal and the question was, "Is this rate reasonable," the railroad would have to come in and prove to the Commissioner that the amount the rate was above 180 percent of available cost was the same as every other rate about 180 percent of variable cost. In other words, you would put on trial not just that one rate, but every rate to every captive shipper to try to prove that you were spreading this burden equitably, and you would bring in every rate below variable rate cost because you would have to make full findings that the railroad was pricing every load below 180 percent—an many as they could.

And so, what we're afraid of there is a process that is going to lead directly into a swamp of paperwork. That's a very long answer to a simple question, but——

Senator **Grassley**. Thank you very much, and I do think that you did a good job of answering my question. This is an approach that deserves some indepth dialog between us.

I'd like to ask you, Mr. Walsh if you remember my conversation with Dean Stoll of the Iowa Public Service when he referred to Burlington Northern shipping coal for Neal 4.

Mr. WALSH. For what, Senator?

Senator GRASSLEY. For Neal 4. That's a utility plant, coal-generated. He said that Burlington Northern had a 93-percent return on investment for delivery of coal there, compared to an overall return of 16 percent on all other rail service. Now, to me, this difference seems abnormally high. I'd just ask for your comment on that.

Mr. WALSH. I'm not a coal specialist, but assuming what he stated was correct, it reaffirms my concern that is we have to lower their rates, which may or may not be reasonable—let's assume they're not reasonable and they have to be lowered. It means for us to get an adequate return on investment, we're going to have to raise these differentially priced commodities, and we can't do that in face of the competition of the marketplace. It simply will not allow us to extract higher freight rates from any of the grain that we handle. And in effect, we will forfeit that grain to other forms of transportation, and we will not be benefited, because as that traffic disappears, more of the burden of cost will shift to this captive-type traffic, if you will, and the rates will again be forced higher. So it's a self-defeating, shoot-yourself-in-the-foot-type of approach.

Senator GRASSLEY. Well, am I supposed to read into that that we're pitting the farmers against the utility users?

Mr. WALSH. I don't think there's any deliberate effort, but I'm not sure they've thought through the process. They're looking at their rates as being very high and the rates that we exercise in the agricultural industry as being low, and that there should be some more reasonableness put into their rates, which by the fact that if that happens it is going to force us to extract more revenue from the other shippers, and it will simply force the railroads out of the market in many cases. And where these shippers are remote from the river or from other forms of transportation, they'll be less competitive in the export market. So I have a great concern, from the standpoint of grain, as to the direct, long-term effects of this bill.

Senator GRASSLEY. Can you comment on the situation described in Mr. Stoll's testimony, where the utility is paying $10.03 per ton for coal under one contract and $14.03 per tone for coal under another contract, for similar mileage, and what would be the difference?

Mr. WALSH. OK. I'm not directly familiar with that, but I do know that since the Staggers Act—and there's been a transitional stage, but I understand about 70 percent of our coal volumes are now under contract, and so there's a movement away from the tariff-type rates, which predate Staggers, to a negotiated type of transportation cost. I would like to believe it is amenable to both parties and considered fair. So without——

Senator GRASSLEY. So this is something that's in transition here? This isn't really comparing apples with apples; is that what you're saying?

Mr. WALSH. It's my understanding—as I say, I'm not directly conversant with these situations—that these things are being negotiated on a contract basis more and more, so that, today, by far the greatest percentage of volume is under contract.

Senator **Grassley**. If there would be a written followup to that, feel free to submit that. You said yourself you have some doubts about whether or not that could be the case as you addressed it; right?

Mr. **Walsh**. I simply have no direct knowledge. That's what I should have said.

Senator **Grassley**. Without the changes advocated by the previous witnesses, when can we expect the ICC to determine railroads to be revenue adequate? It seems to me that the ICC, in the face of the Norfolk Southern $1.2 billion bid for CONRAIL——

Mr. **Walsh**. Well, I think the Burlington Northern has been the only railroad, in my recollection—and this happened, I guess, around 1974—that was able to go into the equity market and sell stock. They sold preferred stock, and that's a reflection of a lack of interest in the business community in an industry that is not making returns on assets that would encourage that kind of investment risk. So it's not just the ICC that is saying this. It's the business community at large that is saying, "You're not worth investing in yet, but you're getting better." And Burlington Northern has got some fairly good marks from Wall Street, but we're not described as a winner in a large sense of the word. They're not rushing to buy our stock.

Senator **Grassley**. Jerry.

Mr. **Conlon**. My answer is, I don't know when the ICC would determine that the railroad industry is revenue adequate, but I think the answer would be when it is—and I think great progress has been made—that the Staggers Act has allowed people to address problems that have been structural and have been helpful. The economy since 1980 has not been helpful, especially for those of us in the Midwest; very especially for those of us which have to haul grain, which is a disaster area not only for the farmers, but also for ourselves. Senator, I'm trying in my mind to understand the question. Is the question whether or not we think they will?

Senator **Grassley**. Yes.

Mr. **Conlon**. Yeah. My opinion is I think they will and that some railroads are approaching that. I wish I enjoyed that. We have some goals at Burlington Northern, if I may add something, Senator, of achieving certain levels of revenue adequacy, and part of that strategy is to depress our costs. So cost control over the Staggers Act is something that is now not only possible, but a preferred way to go, whereas, under previous regulation, it was a simple direct passthrough to customers; if your costs went up, you passed them through. Today, the marketplace will not allow us to do that. We cannot run to the Commission and get wholesale rate increases. That simply will not be absorbed by the market.

Now, the part about Norfolk Southern, I don't think there's a direct linkage. They are acquiring a very large railroad with no debt. So, to that extent, it wouldn't be a direct linkage to the experiences of Norfolk Southern. It would be like they're getting the asset for the money; that's all. And I don't think it's directly attributable to the revenue experiences of Norfolk Southern.

Senator GRASSLEY. Now, a question to kind of put you on the spot, Jerry, would be to refer to coal on the Powder River Basin and the Chicago North Western building a railroad there; $26 million, right?

Mr. CONLON. Oh, this is easier than the tough one, Senator.

Senator GRASSLEY. Now wait. The idea is that competition is going to bring some advantage to the consumers. Now, a lot of people behind 447 would indicate that the effects of 447 would be the same as what you're trying to do in building a railroad, to be competitive with Burlington Northern.

Mr. CONLON. I'm sure there would, Senator. I think it is distinguishable. (1) We're putting money on our line. (2) We're not trying to change the law.

Senator GRASSLEY. I'm saying that the cost of that $26 million would not be as competitive without the cost of that $26 million.

Mr. CONLON. That's not the game we're playing. There's a market out there. We're willing to invest in that market, and we're willing to do it under the law that's in place. The people that I'm disagreeing with, they're saying we want to use your asset and change the law to do it. I think the proof of the pudding is in the eating. We're willing to play on the game that's laid before us. We could lose that one. I hope not. I'm getting tried of losing.

Senator GRASSLEY. Do either one of you have anything in closing that you want to comment?

Mr. CONLON. I just want to thank you very much, and I heard before the statement that Iowa was ably represented, and I certainly agree in this case.

Senator GRASSLEY. Well, thank you.

Mr. WALSH. I've heard it said that the Commission is prorailroad. I always envisioned it the other way.

Senator GRASSLEY. You understand, I didn't make that statement, but I did ask for people to comment on both. It depends on whether you're talking to truckers or railroad. If you're talking to truckers, it's prorailroad, and if you're talking to railroad, it's protruckers. Thank you very much.

STATEMENT OF C.I. MacGILLIVRAY, DIRECTOR, PLANNING AND RESEARCH DIVISION, IOWA DEPARTMENT OF TRANSPORTATION

Mr. MACGILLIVRAY. I'm happy to have the opportunity to visit with you and provide some comments on the part of the Iowa Department of Transportation on Senate Bill 447 (the Railroad Antimonopoly Act of 1985), which seeks to place the rail industry within the scope of antitrust laws.

The Department, for many years, has been extensively involved in concerns relating to the future of the railroad industry in the United States. This past month, the Department of Transportation held 12 public meetings around the State to hear from Iowa rail shippers on their anticompetitive concerns and effects under the Staggers Rail Act. Over 450 invitations were sent to major shippers representing electric utilities, grain elevators, and manufacturing firms, and 32 firms attended these hearings. We found a general acceptance, in this set of hearings of the staggers Act, except from the utilities, but confusion on the intricacies of the Staggers Rail Act.

The size or amount and kind of shipments seemed to be a dividing line for differing opinions. Larger companies and large shippers believed that Staggers is OK and recommended leaving it alone. Smaller shippers felt adversely affected by rate-route and reciprocal switching problems.

For instance, the larger grain shippers had little apparent concern for the confidentiality of grain-shipping contracts and consider themselves secure in their ability to find out what the rates and terms are for a grain shipper along the line. They apparently feel that rates, etc., aren't hurting them because they can adjust within a short time. Small elevator operators, conversely, feel that they have a harder time because they can't find out what someone else is paying for freight rates. These 12 statewide public meetings resulted in the following conclusions:

Electric utilities identified they have experienced problems with the Staggers Act.

Other shippers attending public meetings reported they have experienced relatively few adverse impacts.

There appears to be support for Staggers on general principles.

The confidentiality of shipper-carrier contracts should be retained.

Reciprocal switching charges are felt unreasonable. As a result, a lot of rail business is foregone to trucking.

Abandonments should be permitted if the shippers aren't using the line.

Other than the utility companies, there was no major support for revision to Staggers. At the same time, however, a need was identified for an objective and thorough investigation into the impacts of Staggers resulting from the ICC's manner of implementation. This is needed to eliminate misconceptions or confusion about Staggers, which apparently exists.

The utility companies had a good understanding of the equity and competitive access principles involved with Staggers. They believe the ICC's administration of the Act is not balancing the needs of the captive shippers with the revenue adequacy concerns of the railroads. In particular, the ICC definition of revenue adequacy and market dominance were not supported. Their argument is based on what they see as a failure to guarantee fair and reasonable rates to captive shippers who have no viable alternative means of transportation. Some of what they stated, you also heard today.

I really don't want to become too repetitive, but we did hear about a 2-year span of decreases in coal prices, accompanied by a 12-percent increase in the cost of transportation of coal. We heard that 28 percent of utility charges is directly related to rail transportation costs for coal. We heard the question that you asked: "How can the railroads ever be found to be 'revenue adequate' when the Norfolk Southern, which recently purchased North American Van Lines and is offering to purchase Conrail, can be found to be revenue inadequate?"

On the other hand, we heard the supporters of the ICC's current practices stress that the Staggers Act is working well, and is achieving its overall goal of keeping the railroads viable in the private sector through reliance on the marketplace. They maintain it should not be changed in any way at this time. The information compiled by some of these sources shows that, for instance, since 1972, the average price of coal per ton at the mine has increased over 250 percent, whereas rail coal rates have increased only 120 percent at the same time; that since 1980—passage of Staggers—Iowa utility rates have constantly increased faster than the consumer price index, whereas rail coal rates have consistently increased below the consumer price index; that between January of 1982 and 1985, electric rates have increased over 20 percent, whereas coal rates have increased 6.6 percent.

Now, those are also data based on other sources, not as a result of initial investigations by the department.

The major question appears to be equity for captive shippers. This is raised by both sides, with numbers to back up each argument. Indeed, it seems a further objective study of these issues is needed before a fair assessment can be reached.

So in conclusion, the Department is concerned about the regulatory environment within which the rail carriers must operate, but feels there's no apparent immediate compelling need to open up the Staggers Act. We feel it is imperative that Congress, the States and the Interstate Commerce Commission not walk away from these railroad issues; that Congress be afforded the time to thoroughly assess the entire spectrum of competition in the rail industry. We suggest that Congress explore the situation in further detail and develop a more extensive background. Only through additional efforts can reasonable long-term solutions in the area of rail competition and rail regulation be identified, evaluated and implemented. And if effective studies are not forthcoming, Congress may be in the position of having to compel them to be completed.

Senator, with that, I submit to any questions that you have.

Senator **Grassley**. Well, sure. And I do have questions. First of all, let me give you a general thank you. Not just you, but to other personnel that you deal with; some of them under you and some of them on the same level. We've appreciated the analysis of the transportation changes being made in Iowa, plans as they've been at the national level and now they have affected people in Iowa. We wait, generally, until we get some sort of a view from you; because we consider it a very important part of our input as we make decisions on transportation. And consequently, that's one of the reasons we asked you to be here. It's really important that I would specify that that be applicable to this issue right here.

The 12 hearings that you held around the State and the review of the issue by the Nation's No. 1 State transportation department has been helpful in bringing this issue to a forefront, and we appreciate that assistance here specifically, but also in the general vein.

Do you feel that we have a serious problem in our State, or are our railroads treating our shippers fairly?

Mr. **MacGillivray**. The evidence that we received in conversations and meetings with our shippers does not indicate any problem of a severe nature—discrimination or any other problems. With invitations to over 450 people, and no major problems identified, we don't seem to be able to identify a concern to bring to your attention.

Senator **Grassley**. Maybe you said so in your statement, but do those 450-some people that you've had contact with include some of the industries represented here today: utilities, grain elevators and agribusinesses. That figure included some or all of those industries?

Mr. **MacGillivray**. To the best of my knowledge, it included all of the industries represented today.

Senator **Grassley**. According to its supporters, S. 447 promotes competition as an approach to resolve shippers' issues to switching of railroads. Do you think this approach would be a useful complement to the benefits of deregulation that railroads enjoy under the Staggers Act?

Mr. **MacGillivray**. Senator, we did not discover any support or solution to the concerns that were identified, that would come from what's identified in 447. We did not hear that type of support.

Senator **Grassley**. This is a followup question. Could that same answer be applicable to 477, if you're familiar with that?

Mr. **MacGillivray**. I'm not quite as familiar with 477. I have some knowledge of it. It was not as much a subject of major discussion. However, in reflecting upon what we did hear, I think the conclusion would be somewhat similar.

Senator **Grassley**. Under our present system, a shipper must pursue a disagreement through the ICC. If he is unhappy with an ICC determination, what are his options for relief?

Mr. **MacGillivray**. Senator, I'm not enough of an expert practitioner with the ICC to really have an answer to that.

Senator **Grassley**. Could have your legal department send a response?

Mr. **MacGillivray**. I would be glad to ask our department legal staff to take a closer look at that question.

Senator **Grassley**. OK.

Mr. **MacGillivray**. Senator, I might add that there are other remedies, of course, back in the marketplace that are well known and available.

Senator **Grassley**. Why don't I just give you that. That's No. 3. That was my final question, and I want to thank you for coming.

In conclusion, I want to thank all who participated in today's meeting. I feel that all input will help in dealing with this issue. And ever since I've been in public service, particularly the last 15 years of that public service, I think Iowa has faced a problem with its rail service. Our the years, we've lost railroads through bankruptcies, mergers, and rail abandonment to many Iowa communities. It seems to me that we're just now getting ahead of the ball game, as far as rail service is concerned. Our railroads seem to be stronger, yet some of our shippers are concerned with the results of a less competitive atmosphere, and that's something that we're dealing with here.

We will not be able to reach a final conclusion here today, and this hearing wasn't intended to do that. But I will review the comments and take them into consideration as the judiciary committee reviews the future of antitrust in connection with the ICC and the Staggers Act, and I want to repeat that the record will remain open for 14 days for further comment and consideration of additional points of view.

And so, again, I thank you all for coming, and the meeting is adjourned.

[The hearing was concluded at 4:35 p.m.]

[Prepared statement follows:]

BEFORE THE
SUBCOMMITTEE ON ADMINISTRATIVE PRACTICE AND PROCEDURE
OF THE UNITED STATES SENATE COMMITTEE
ON THE JUDICIARY

REGARDING: SENATE BILL 447

PREPARED REMARKS
ON BEHALF OF THE
IOWA DEPARTMENT OF TRANSPORTATION

I. Introduction

The Iowa Department of Transportation is pleased to have this opportunity to present its comments on Senate Bill 447 (the Railroad Antimonopoly Act of 1985) which seeks to place the rail industry within the scope of the antitrust laws.

The Iowa DOT for many years has been extensively involved in concerns relating to the future of the railroad industry in the United States. It has been a participant in the railroad rationalization and restructuring process since 1974. The department has participated extensively in federal and state courts and before the ICC regarding the Rock Island bankruptcy and liquidation, the Milwaukee Road reorganization, major rail mergers such as the Union Pacific, Missouri Pacific and Western Pacific unification, sale of Conrail, and various ICC rule making proceedings, also federal railroad assistance funding and a variety of other matters. As a consequence of this varied experience with railroad issues, Iowa DOT believes that it is appropriate to record the following general remarks regarding Senate Bill 447.

II. Staggers Act in Iowa

On August 8, the Iowa DOT held 12 public meetings around the state to hear from rail shippers on the anti-competitive concerns and effects under the Staggers Rail Act. Over 450 invitations were sent to major shippers representing electric utilities, grain elevators and manufacturing firms, and 32 firms attended. We found a general acceptance of Staggers (except for the utility companies) but confusion on the intricacies of the Staggers Rail Act.

There was general support for Staggers, but some of the shippers had little experience with the Act. Many of the shippers have not had any negative experience with these issues.

The size or amount and kind of shipments seemed to be a dividing line for differing opinions. Larger companies believed Staggers is okay--leave it alone. Smaller shippers felt adversely affected by rate/route and reciprocal switching problems. Some grain shippers believed that grain companies and buyers are profiting from the ability to contract for freight rates and that very little, if any, of the savings obtained through contracts is passed along to local elevators or producers.

The larger grain shippers had little apparent concern for the confidentiality of grain shipping contracts and consider themselves secure in the ability to find out what the rates and terms are for a grain shipper along the line. They apparently feel that the rates, etc. aren't hurting them because they can "adjust" within a short time. Small elevator operators feel they have a harder time because they can't find out what someone else is paying for freight rates. These 12 statewide public meetings resulted in the following assessment:

- Electric utilities have experienced problems with the Staggers Act and have been actively involved in reforming the Act or the ICC implementation of the Act.
- The other shippers attending these public meetings have experienced relatively few adverse impacts resulting from implementation of the Staggers Act.
- There appeared to be support for Staggers on general principles.
- Depending upon volume and nature of shipments, there exists a difference of opinion regarding what, if anything, is wrong with Staggers.
- Confidentiality of shipper/carrier contracts should be retained.
- Reciprocal switching charges are unreasonable. As a result, a lot of business is foregone to trucking.
- Abandonments should be permitted if the shippers aren't using the line.
- Staggers should be made to work but there is an ambivalence as to how.

Other than the utilities, there was no major support for the revision of Staggers. At the same time, however, a need was identified for an objective and thorough investigation into the impacts of Staggers resulting from the ICC's manner of implementation. This is needed to eliminate misconceptions or confusion about Staggers which apparently exist.

The power companies had a good understanding of the equity and competitive access principles involved with Staggers. The utility companies strongly believe that the Interstate Commerce Commission's (ICC) administration of the Act is not balancing the needs of the captive shippers with the revenue adequacy concerns of the railroads. In particular, the ICC definitions of revenue adequacy and market dominance were not supported. They state Congressional action may be necessary if ICC action is not corrected to provide protection to captive shippers. The majority of utility companies in Iowa see themselves as captive shippers and feel they are thus more susceptible to rail rate increases, due to a lack of negotiating power or adequate protection through regulatory channels. Their argument is based on what they see is a failure to guarantee fair and reasonable rates to captive shippers who have no viable alternative means of transportation.

The utilities stated:

1. From 1982 to 1984, the price of coal at the Powder River Basin's Sunedco mine decreased by 35 percent. The cost of transporting that coal, however, increased by 12 percent during the same period.

2. Coal is the fuel used to produce over 53 percent of the nation's electricity each year and a full 85 percent of this coal comes from mines served by a single railroad.

3. Over 28 percent of electric utilities' total production cost is rail transportation charges for coal.

4. How can railroads ever be found to be revenue adequate? The Norfolk Southern which recently purchased North American Van Lines for $315 million and has offered $1.2 billion for Conrail, has been found by the ICC to be revenue inadequate.

On the other hand, supporters of the ICC's current practices stress that the Staggers Act is working well in achieving its overall goal of keeping the railroads viable in the private sector through reliance on the marketplace. They maintain it should not be changed in any way at this time. Information compiled from such sources shows:

1. Since 1972, the average price of coal per ton at the mine has increased over 250 percent, whereas rail coal rates have increased only 120 percent during the same period.

2. Since 1980 (passage of Staggers) Iowa's utility rates have been constantly above the consumer price index, whereas the rail coal rates have been consistently below the consumer price index.

3. Between January 1982 and January 1985 electric rates have increased 20.8 percent, whereas coal rail rates increased only 6.6 percent.

The major question is equity for captive shippers; this is raised by both sides with numbers to back up each argument. Indeed, further objective study of these issues is needed before a fair assessment can be reached.

III. Conclusion

The Iowa DOT is concerned about the regulatory environment within which rail carriers must operate in. There is no apparent immediate compelling need to open up the Staggers Rail Act. It has apparently worked well for railroads and has enabled them to compete more effectively for intermodal, especially truck, traffic. One shipper noted that the Act was passed just at the start of a decline in traffic because of the general economy. It has enabled the railroads to capture traffic that they would not have carried prior to the Staggers Rail Act. One cannot help but wonder, however, how well the various provisions of the Staggers Rail Act will be used by the carriers (and in future decision of the ICC) during a period of economic growth. However, we feel it is imperative that Congress, the states and the ICC not walk away from these railroad issues. Congress must be afforded the time to thoroughly assess the entire spectrum of competition in the rail industry. Congress may need only to enact corrective legislation on the rules which the ICC uses regarding competitive access and rate equity but should not now scrap the entire existing process. Iowa strongly suggests Congress explore this situation in further detail and develop a more extensive background. Only through additional efforts can reasonable long-term solutions in the area of railroad regulation be identified, evaluated and implemented. If effective studies are not forthcoming, Congress may have to compel them to be completed.

C. I. MacGillivray, Director
Planning and Research Division
Iowa Department of Transportation
800 Lincoln Way
Ames, IA 50010

NIPCO
NORTHWEST IOWA
POWER COOPERATIVE
P O Box 240
Le Mars, Iowa 51031
Phone 712 546 4141

August 26, 1985

The Honorable Charles Grassley
United States Senate
Washington, D. C. 20515

Sir: In Reply Refer To: Code 100

SUBJECT: Submission of Resolution Relative to S.477 - Amendment to Sherman Anti-Trust Act

Northwest Iowa Power Cooperative, aka NIPCO, as a member of the Mid-West Electric Consumers Association (MECA) has in past years played a very important part in the development of "resolutions" by which MECA operates. At MECA's December, 1984, Annual Meeting the enclosed resolution was unanimously adopted supporting legislative initiative to restore competition in railroad coal transportation.

NIPCO is greatly concerned about excessive freight rates because of the costs incurred in shipping western coal to the Neal 4 generating station located on the Missouri River south of Sioux City.

Therefore, in support of legislation to correct the inequities in the 1980 Staggers Rail (Deregulation Act), NIPCO herewith submits the enclosed resolution for the written record at your August 29th hearing on S.447. We respectfully request this resolution be included in the written record of the hearing on behalf of the Northwest Iowa Power Cooperative.

Sincerely,

NORTHWEST IOWA POWER COOPERATIVE

Philip A. Hauan
General Manager

PAH:SRM

Enclosure

"TEAM SPIRIT '85"

RESOLUTION 22

RAILROAD DEREGULATION AND WESTERN COAL

RAILROAD FREIGHT RATES

WHEREAS, this nation's energy policy -- as well as common sense -- has encouraged the use of coal available in relative abundance in the United States in order to reduce our dependence on foreign oil thus reducing inflation and our balance of payments deficit; and

WHEREAS, western coal production, increasing annually, must continue to increase if the nation is to meet its real energy needs, and for this to occur a large portion of this coal must be hauled by the nation's railroads so it can reach its point of use reliably and expeditiously; and

WHEREAS, the 1980 Staggers Rail (Deregulation) Act, as it has been implemented through various actions and proceedings of the Interstate Commerce Commission (ICC) provides virtually no protection for captive shippers (of ore, grain, and other bulk products, particularly coal, which are limited to a single railroad for transportation to market or point of use) and surely will result in excessive freight rates with resultant increases, in the case of coal, in the cost of electric power for utility customers; and

WHEREAS, these excessive freight rates will serve to thwart a national energy policy which relies heavily on relatively low-cost domestic coal reserves, and will unnecessarily delay the needed shift from oil to coal use in the nation's electric generating systems;

NOW, THEREFORE, BE IT RESOLVED, that Mid-West Electric Consumers Association (Mid-West) supports joint efforts by the National Rural Electric Cooperative Association (NRECA), the American Public Power Association (APPA), and Western Fuels Association, Inc., to take whatever steps offer the best chance of success in neutralizing the monopoly power of railroads and set aside excessive coal freight rates, including seeking legislative relief, participating in ICC proceedings affecting railroad coal shipping rates and conditions where indicated, including appeals to the courts, and urges them and other interested groups to pursue these goals without letup; and

BE IT FURTHER RESOLVED, that Mid-West supports Western Fuels' legislative initiative to restore competition in railroad coal transportation, even where railroads have a monopoly, through amendment of the Sherman Antitrust Act in bills similar to bills introduced by Senator Dennis DeConcini of Arizona, Max Baucus of Montana and Alan Simpson of Wyoming (S.2417), and Rep. John F. Seiberling of Ohio, Byron Dorgan of North Dakota, Pat Williams of Montana and others (H.R. 44559) in the 98th Congress, and urges that a renewed effort be made during the next Congress.

tfi FERTILIZER NEWS RELEASE
The Fertilizer Institute • 1015 18th St. N.W. • Washington, D.C. 20036
(202) 861-4900 • Telex 89-2699

Contact: Donald N. Collins
Thomas E. Waldinger

Railroads Should Be Subject to Antitrust, Spokesman Says

FOR IMMEDIATE RELEASE

WATERLOO, Iowa, August 29, 1985 -- Rail carrier actions to unilaterally cancel joint rates, and eliminate or restrict reciprocal switching arrangements have resulted in the growth of railroad monopoly power and the need for complete deregulation, according to a spokesman for the fertilizer industry in a congressional field hearing chaired by Sen. Charles Grassley (R-Iowa).

Bob Stone, managing director of physical distribution for Terra Chemicals International, and a member of The Fertilizer Institute's Transportation Committee, told the Senate Judiciary Committee that railroads are taking full advantage of a partially deregulated environment in which they still enjoy antitrust immunity.

"These exemptions are most noticeable when railroads take anticompetitive action to keep traffic on their long-haul routes," Stone said. He quoted a rail industry executive who acknowledged the "monopolizing grip" of carriers who control both the origin and destination of rail traffic.

Stone said railroads have tightened that grip by cancelling or limiting agreements on joint rates and reciprocal switching. Such agreements are traditionally sought when shippers desire to switch from an originating carrier to one or more alternate carriers at lower rates and more direct routes. When allowed, the railroads negotiate a "joint" rate for the product's movement, and offer reciprocal switching from their rail line to the competitive carrier. By cancelling these arrangements, Stone said, originating carriers are driving out competition and forcing shipper reliance on a single rail line.

He cited the major phosphate mining locations in the Bone Valley region of Florida, all served by one rail carrier, the Seaboard System. The nearest competitor, 200 miles away, is the Southern Railroad. Prior to rail deregulation in 1980, Stone said, a connecting track -- the Jacksonville gateway -- offered shippers a competitive alternative between the two rail lines, and provided a rate negotiation tool. Since deregulation, he said, Seaboard closed the Jacksonville gateway, leaving shippers with no alternative to the Seaboard System.

"Such action is clearly in violation of the spirit of the antitrust laws, but is permitted under the Interstate Commerce Act," Stone said.

The industry executive offered support for Senate bill S.447, legislation to apply antitrust laws to the rail industry.

The Fertilizer Institute represents, by voluntary membership, more than 90 percent of the nation's fertilizer industry. Producers, manufacturers, retailers, trading firms, and equipment manufacturers who comprise its membership are served by a full-time Washington, D.C. staff in various legislative, educational and technical areas, as well as with information and public relations programs.

THE RAILROAD ANTIMONOPOLY ACT OF 1985
S. 447

TUESDAY, SEPTEMBER 24, 1985

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 10:10 a.m. in room SD-628, Dirksen Senate Office Building, Hon. Strom Thurmond (chairman of the committee) presiding.

Also present: Senators Simpson, Grassley, Specter, McConnell, and DeConcini.

Staff present: Kenneth Starling, antitrust counsel; Jodi Brayton, counsel to Senator Simpson; Alice Milder, counsel to Senator Grassley; Richard Holcomb, counsel to Senator Denton; Victor Maddox, counsel to Senator McConnell; and, Robert Feidler, minority counsel.

OPENING STATEMENT OF SENATOR ALAN K. SIMPSON

Senator SIMPSON [presiding]. The hearing will come to order.

Senator Thurmond is delayed in the Senate and I have to preside over the Senate at 10:30, so I will be leaving shortly, but I want to commend the chairman, Senator Thurmond, as I often do, for the many things he does and has done for me, and for holding this hearing on S. 447, the Railroad Antimonopoly Act of 1985.

[The opening statement of Chairman Thurmond follows:]

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

Today is the second hearing on S. 447, a bill introduced by Senator DeConcini, who is a distinguished member of our committee.

The bill before us is intended to address a situation faced by some shippers of bulk commodities on railroads. The shippers in question are usually located on or near the tracks of only one railroad and are thus "captive" to that railroad.

With the deregulation of the railroads following passage of the Staggers Act, railroads have been given the flexibility to engage in differential pricing. This means that the railroads may now charge different prices to shippers in different markets, in response to the degree of competition faced by the railroads in each market. This differential pricing has led to calls for protection by shippers in markets in which the railroads face reduced competition.

At our last hearing, the administration indicated its opposition to the bill, suggesting that current monopolization law, ICC procedures and Staggers Act protection are adequate to deal with the problems of captive shippers. Since that time, Senator DeConcini has been working on revisions to his bill, and today we will hear testimony about the purpose of the bill and the nature of the revisions.

We welcome our distinguished witnesses and look forward to their testimony.

Senator SIMPSON. It is a measure which I have great interest in, and I am a cosponsor, and I admire the Senator from Arizona, Senator DeConcini, as he has worked with me on this, and it is not something that we want to see slip into the "vat," somewhere along in the process here.

It is intended to address a situation faced by some shippers of bulk commodities. Now railroads, by providing a remedy under the antitrust laws, when a rail carrier of course would appear to take advantage of a, quote, "captive shipper," unquote, and of course there is no need for me to go on and define all of the ramifications of that, but that is a shipper with no alternative means to get his goods to market.

And that is the case with many, or at least some of our coal producers, and my State happens to be the third largest coal-producing State in the United States.

That may shock some, but it is very real, and we are only a very few thousand tons behind the second State in coal production, some 114 million tons a year, and we need alternative forms, when we have coal in the ground, and after mining it, a certain figure per ton, and then watch that almost triple by rail rates.

That is not good for the balance of trade, it is not good for exporting States, and it is one thing that I intend to address.

And there are certain agricultural products, and we will hear about that today, that are affected. Chemical products. In fact the "captive shipper" issue, or problem, can exist with nearly every product which is shipped in bulk, and indeed, under previous railroad deregulation legislation, before our act of 1976, and the Staggers Rail Act of 1980, the railroad industry was subject to pervasive regulation by the ICC, especially rate regulation.

I do not intend to recapitulate that history but I think one point needs to be emphasized, and that is that during most of the period that antitrust laws were evolving, the railroads, because of regulation, were treated in a special manner when it came to application of the antitrust laws, and it would be certainly incorrect to characterize railroads as a wholly exempt industry, but numerous statutory and judicial exemptions in fact were created.

And while that has certainly been altered drastically by recent legislation, key antitrust exemptions that were products of an earlier era still remain in place, notably section 16 of the Clayton Act and the famous Keogh doctrine.

So although because of this anomaly, railroad deregulation, although largely successful, has not always worked as planned.

While market forces have restrained prices where effective competition exists, the trend toward consolidation necessarily reduces the number of competitive situations and that vexes many of us. At the same time, the railroad antitrust exemptions hamstring the ability of shippers to use the antitrust remedies that are supposed to restrain market-dominant industries.

So I do take pleasure in cosponsoring S. 447 and in swift summary, the bill is designed to restore a competitive balance in the rail industry, not through reregulation of rates, but by insuring competitive rail access to the facilities of otherwise rail-captive shippers, and by eliminating certain antitrust exemptions that the railroad industry currently enjoys, and here, by creating this antitrust violation of the abuse of the captive shipper situation, we have created a mechanism that does not require the intervention of a Federal agency.

An aggrieved party can simply take his case to court, and if he is wronged, or, it is wronged, then receive relief in the form of damages or injunction, or whatever the court may deem appropriate.

The threat of litigation and the threat of being found liable for damages acts, in my mind, as a very strong deterrent against abuses with regard to the captive shippers.

And so, I am very pleased to support this and want to pay careful attention as it wends its way in this curious arena. And so with that, I want to say that Senator Thurmond has a statement to make, and I would order that that be entered into the record as if read in full, and prior to my remarks, and it may be that my good colleague from Arizona may have a statement to make in connection with this hearing before we go to the first witness.

Senator DECONCINI. Mr. Chairman, thank you. I want to join you in publicly acknowledging Senator Thurmond, the chairman of the committee, for his continued willingness to accommodate members on some specific bills that have been introduced.

I also want to thank him for his leadership in this role. Today's hearing, as the chairman knows, is the second, and I assume the final day of hearings on S. 447, the Railroad Antimonopoly Act of 1985.

At our first day of hearings last April, the committee heard from a wide array of witnesses, both pro and con, and it was clear from that day of hearings that a problem does exist concerning equitable treatment between rail carriers and captive shippers.

It was less clear what the best solution should be. In the intervening months, since the first day of those hearings, numerous meetings with interested parties have occurred, during which we have attempted to address the criticisms of the original bill.

I believe the August 8 draft, which has been widely circulated, reflects the latest thoughts on the bill and meets many of the objections raised earlier. In essence, the bill has been narrowed considerably to subject railroads to the Sherman Act, in a very limited manner.

The bill as now drafted would overturn the *Keogh* decision with respect to section 2 of the Sherman Act. It would allow injunctive relief and would legislatively recognize an essential facility doctrine with respect to railroads.

We have an excellent group today of witnesses and I hope that I can stay to hear all of them. Unfortunately, the Appropriations Committee is meeting and I have to be there at the same time.

In light of the chairman's absence, I will continue.

Senator DECONCINI [presiding]. The first panel will consist of William Fogarty, administrator, transportation division, State of Montana; John Bagalay, Milan Yager, and Don Johnston. Will they all come forward, please, and take their seats. Please identify yourselves for the record. We will start with Mr. Fogarty.

Gentlemen, because of the time restraints, please summarize your statements, and we will put them in the record in complete form. Then I will ask some questions for clarification purposes. Please proceed.

STATEMENT OF A PANEL CONSISTING OF WILLIAM FOGARTY, ADMINISTRATOR, TRANSPORTATION DIVISION, DEPARTMENT OF COMMERCE, STATE OF MONTANA, HELENA, MT; JOHN BAGALAY, GENERAL COUNSEL, LOWER COLORADO RIVER AUTHORITY, AUSTIN, TX, ON BEHALF OF THE AMERICAN PUBLIC POWER ASSOCIATION; DON M. JOHNSTON, DIRECTOR, UNITED FRESH FRUIT & VEGETABLE ASSOCIATION, JOHNSTON FARMS, EDISON, CA, ACCOMPANIED BY DICKSON LOOS, UNITED FRESH FRUIT & VEGETABLE ASSOCIATION, ALEXANDRIA, VA

Mr. FOGARTY. Thank you, Mr. Chairman, members of tbe committee. My name is Bill Fogarty. I am the administrator of the transportation division in the Montana Department of Commerce, and I appreciate the opportunity this morning to supply testimony in support of Senate bill 447.

Montana's rail system consists of approximately 3,500 route miles of track operated primarily by three class I railroads, the Burlington Northern, the Soo, and the Union Pacific, and two recently born short line carriers.

Of this total, approximately 825 miles are branch lines. The dominant carrier is the Burlington Northern, which operates over 91 percent of the route miles covering all portions of the State. The Burlington Northern serves 98 percent of the grain elevators in Montana, and all the elevators with 26 and 52 car facilities, with the exception of a 52 car facility at Butte, which is on the Union Pacific System.

Since 1979, the BNRR has abandoned 16 lines constituting a total of 400 route miles. Ten of these lines have been abandoned since 1983. In addition, the 66 mile Spring Creek Junction to Geraldine line was transferred to the newly created Central Montana Rail short line, as a result of a lawsuit settlement between the State and the Burlington Northern.

An agreement recently consummated between the Butte, Anaconda & Pacific, and the State of Montana, resulted in the creation of RARUS, a new company that will operate a short line railroad in southwestern Montana, including over 43 miles of trackage previously served by the Butte, Anaconda & Pacific.

On their system diagram map, the Burlington Northern currently has one line in category 1. That is the lines they are currently preparing abandonment applications on, constituting 28 route miles. Two lines are in category 3, constituting 15 miles.

The total number of miles abandoned by all carriers in the State since 1979 is 1,251 miles.

Beside the socioeconomic hardships caused to producers, shippers, and businesses along the lost branch lines, the impact on the areas' road systems caused by the diverted rail to truck traffic is devastating. On just one 66 mile branch line serving a grain area in central Montana, the State estimates the annual added highway impact costs to be at least $4.6 million.

From exhibit I, the map of Montana's rail system, you will note that the BN trackage virtually blankets Montana, with the minor exceptions of the Soo Line in the extreme northeast corner, and the Union Pacific branch line in the extreme southwest corner.

Upon comparing Montana's grain rates to States such as Colorado, Kansas, and Nebraska, our rates are consistently higher on a per car mile earning basis when comparing hauls of like commodities and distances.

For example, in exhibit II, single car rates on a per car mile earnings in Montana, range from $.48 to $1.60 per hundredweight higher. The increased revenues to the railroad from Montana's excessive rates on 26 car shipments range from $10,062 to $21,866, and on 52 car shipments from $25,480 to $45,760.

In Montana, Burlington Northern's revenue to variable cost ratio on hard red wheat is 240 percent compared to BN's average earnings in other States on hard red wheat of 185 percent.

Carriers other than Burlington Northern moving hard red wheat to the Pacific Northwest earn an average of 114.3 percent of revenue to variable cost.

Let me clarify this with an example used by the BN in September 1984 before the Senate Judiciary Committee.

The BN grain rate from Omaha, NE to the Pacific Northwest ports and from Wolf Point, MT to the Pacific Northwest ports, BN earned $2.90 per car mile out of Montana, and $1.55 per car mile out of Nebraska, and this was compared to a haul from Wolf Point to Portland of 1,087 miles, and from Omaha to Portland of 1,880 miles.

The facts show that BN's rate in Montana is 4.5 percent higher than Omaha, but they earn 80.8 percent more per loaded ton mile and 86.6 percent more when put on a per car mile earnings basis.

The Anaconda Minerals Co. curtailed their mining operations in the Butte-Anaconda area in 1980, causing the loss of approximately 1,500 jobs.

A port authority was established at Butte as a means of promoting economic development. The port moved a variety of products including talc, lumber, rubber, chemicals, and pelletized hay for export. Despite being in close proximity, approximately 7½ miles to the Union Pacific. The port has been virtually unable to utilize this connection because of the exhorbitant switching charges, a minimum of $640 per car that the Burlington Northern Railroad imposes. For the record, Mr. Chairman, I would like to include the testimony of Don Peoples who is the chief executive officer of Butte-Silver Bow, as part of the record.

Senator DECONCINI. Without objection it will appear therein.

[The statement follows:]

STATEMENT OF
DON PEOPLES, CHIEF EXECUTIVE OFFICER
BUTTE-SILVER BOW, MONTANA

THE JUDICIARY COMMITTEE
U.S. SENATE

September 24, 1985

House Committee on the Judiciary Subcommittee
on Monopolies and Commercial Law
July 25, 1985

Mr. Chairman, Members of the Committee, I am Don Peoples, Chief Executive Officer of Butte-Silver Bow, the consolidated city-county government of Butte and Silver Bow County, Montana. I am also the immediate past-President of the Montana League of Cities and Towns.

I appreciate the opportunity to testify on H.R. 1140. This legislation is of great interest to Butte-Silver Bow and many other municipal and county governments around the country. In particular, cities and counties who are "captive shippers" have a great interest in some form of relief from the monopoly pricing that railroads currently enjoy.

Most cities and towns in Montana fall into the category of captive shippers. The dominant carrier is the Burlington Northern Railroad (BNRR) which operates over 91 percent of the rail miles in the state. The BNRR serves 98 percent of the grain elevators in Montana and all the elevators with 26 and 52 car loading facilities with the exception of a 52 car facility at Butte on the Union Pacific System.

The BNRR also dominates the coal shipments out of Montana with 100 percent of outbound coal rail traffic and nearly 100 percent of all coal movements. In fact, about 96 percent of BNRR's total coal traffic originated in the Powder River Basin of Montana and Wyoming. Coal provided over 40 percent of the BNRR's freight revenues in 1984 compared to just over 14 percent for grain. Obviously, Powder River coal is a very lucrative market for BNRR, particularly because it is a largely captive market. In fact, the operating income of BNRR rose 34% (to $979 million) in 1984 because of improved traffic volumes, including a 10.6 percent increase in the number of coal cars loaded. If you wonder why grain and coal shippers are so concerned with competition, consider that the BNRR earned $4.06 billion in 1984. I will comment further on the Powder River Basin later in my statement.

First, let me speak specifically about Butte-Silver Bow and the problems being a captive shipper presents for our economic development efforts.

We are one of the very few areas of Montana that is served by two Class I railroads, the Burlington Northern and the Union Pacific. We also have a short line railroad, RARUS, that formerly operated as the Butte, Anaconda & Pacific (BA&P) Railroad.

Most of the bulk cargo moving in and out of Butte-Silver Bow is handled by the Port of Montana. The Port moves a variety of products including talc, lumber, rubber, chemicals, and pelletized hay for export. Despite being in close proximity (approximately 7.5 miles) from the Union Pacific rail, the Port of Montana has been unable to utilize this connection because of the exorbitant switching charges the Burlington Northern imposes.

Let me give you a specific example. The Port of Montana has the capacity to load lumber from western Montana whose greatest market is to the south, primarily California. The most direct route would be to the south on Union Pacific. (See attached letter from Burlington Northern for reference.) The Port of Montana located just east of Butte, Montana, requested from the Burlington Northern a switch charge which would allow the Port to have access to markets which are currently served by the Union Pacific. The actual switch would take place just west of Butte or about 7.5 miles from the Port facility. In other words, the Union Pacific would have to traverse 7.5 miles of Burlington Northern track in order to provide the necessary service.

As can be seen from the attached letter, Burlington Northern would agree to allow this activity for $ .80/hundredweight (cwt) on a minimum weight of 80,000 pounds for a per car revenue of $640.00. Also, if the Port had an order for a 50,000 pound shipment, they would still be forced to pay the $640.00 because this is based on a 80,000 pound minimum charge.

I am aware that a number of switches are performed for $17.00 to $20.00. The actual switch charge on lumber at Gibbs, Idaho, is $150.00.[1]

The only alternative that the Port of Montana and Butte-Silver Bow have is to take advantage of the more direct route on Union Pacific by constructing an entirely new storage and loading facility just eight miles to the west.

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[1] Burlington Northern tariff 8035-D, Item 1480

As it now stands, the Port of Montana is captive to the Burlington Northern. We believe that H.R. 1140 would go a long way toward offering competition to Butte-Silver Bow's rail movements. Enactment of the legislation would also save Butte-Silver Bow and the Port of Montana millions of dollars that would otherwise be spent on the construction of new loading facilities just eight miles distant from the present facility.

Butte-Silver Bow's difficulties as a captive shipper are not an isolated case in Montana. Because the Burlington Northern controls 91 percent of the rail in Montana, there are a number of other areas where competition, or the potential for competition, would serve to moderate the rates Montana shippers are now forced to pay. This will allow our products to be more market competitive.

Let me return to the example of the coal-rich Powder River Basin in Montana and Wyoming. The Powder River Basin is a perfect example of how a little competition can dramatically moderate rail rates.

In late 1983, the BNRR accepted a federal order allowing the Chicago & Northwestern Railroad to buy half-interest in a 93 mile rail line in the heart of the Basin. With this access, the two railroads share the same rail line, but now compete for coal hauling contracts. Under this competition one BNRR coal customer in Louisiana estimates they will save about $500 million in freight rates over the next 15 years.

I believe that S. 447 will clear the way for competitive for many other Montana shippers with similar benefits in rate reductions. Montana shippers are not the only beneficiaries. Coal customers throughout the country, who often pay 55 to 60 percent of their delivered costs of coal in transportation rates, would welcome the competition.

For example, I am also aware of some other significant transportation problems currently facing our state which could be somewhat alleviated through passage of the bill. Dr. Dennis O'Donnell, professor at the University of Montana, was commissioned by the Missoula County Board of Commissioners to assess Missoula, Montana's place in the Pacific Northwest Intermodal Freight Network. Among his findings was the fact that the Missoula-Chicago route has a rate per mile that is 67 percent higher than the Seattle-Chicago route (i.e., $ .89/mile versus $ .53/mile).

In terms of miles, the Seattle-Chicago route at 2,245 miles versus the Missoula-Chicago route at 1,680 miles is 33.6 percent greater or some 565 miles longer. In other words, while the Seattle-Chicago route is significantly longer, the revenue generated on the Missoula-Chicago run is 67 percent greater.

This simple comparison indicates a problem for Missoula and other intermediate points such as Butte. While the ultimate purpose of Professor O'Donnell's study was not aimed at this particular problem of competitive access, the problem of rate disparities between Montana versus other areas was highlighted throughout his study. If competitive access were to become a reality and true competition existed in Montana, our exorbitant rate structure would surely become more realistic in terms of a relationship of costs to revenues.

Other important conclusions reached by Dr. O'Donnell were:

1. Freight rates for containerized commodities routed through Missoula, Montana, are at least 58 percent higher than the same commodities shipped directly from the Pacific Coast to Chicago.
2. The freight rate differential against Missoula, Montana, is due to the cost of rail shipment on the Burlington Northern originating in Missoula. The Burlington Northern is a monopoly provider of rail services to Missoula and most Montana shippers.
3. Economic development in Missoula, Montana, that depends on freight rates is significantly reduced due to the shipper costs associated with the Burlington Northern.
4. A 58 percent reduction in Missoula-Chicago containerized freight rates on the Burlington Northern would be justified. It would approximate competitive conditions in a market economy and would lead to the development of an efficient transportation system service serving the economic region of western Montana.

In conclusion, Mr. Chairman, I want to stress how important S. 447 is for captive shippers to assist them in obtaining reasonable freight rates and dealing with the monopolistic pricing philosophy of the railroad. The economic development efforts of Butte-Silver Bow and local governments across the country will continue to be hampered by excessive rail rates set where effective competition does not exist.

BURLINGTON NORTHERN RAILROAD

SALES and SERVICE DEPARTMENT
Area Sales Office

800 First Northwestern Bank
175 North 27th Street
Billings, Montana 59101

January 7, 1985

Richard L. Monaghan - Gen. Mgr.
Port of Montana
P. O. Box 3641
Butte, Mt. 59702

Dear Dick:

As a follow up to our December 6, 1984 meeting, and confirming our phone conversation of January 4, 1985, we wish to offer the following box car lumber rate from Butte, Mt. to Silver Bow, Mt.

> 80¢ per cwt, Min. wt. 80,000 lbs to apply in boxcars exceeding 50 ft., but not exceeding 52 ft. 8 inches. with a capacity less than 5600 cu. ft. Subject to six month expiration date.

If you wish this quote issued please advise within 60 days and we will have it issued and effective in a matter of a couple of days.

Yours truly,

TJ Kinney

T. J. Kinney
Area Manager Sales & Service

cc: R. L. Lassiter
    G. D. Schlaeger
    T. R. Jarnigan

TJK/ht

NOTE: Minimum rate for switch and to move box car a distance of 7.5 miles is $640 from Butte to Silver Bow.

For comparison, switch rate for lumber at Gibbs, Idaho is $150 per car in Burlington Northern tariff 8035-D, item 1460.

Mr. FOGARTY. Thank you. In 1981, the Montana grain producers filed a class action suit against the Burlington Northern stating that the grain rates in effect for the period of 1978 through 1980 were excessive.

An ICC law judge in December of 1981 determined that the BN did have market dominance in Montana, and that some rates were as high as 292 percent of revenue to variable costs.

The BN then appealed the case to the full ICC. The ICC failed to make a decision on the case for approximately 2 years.

In 1984, the ICC reopened the entire case saying market dominance and rate reasonableness had to be reproven under the definitions currently in place.

The Montana grain producers have spent over $400,000 to cover expenses on the case thus far. The last Montana's legislative session approved an additional $310,000 for the State to assist in the case for the next 2 years.

The ICC, through its delays and prorailroad bias, have done nothing to protect the captive shipper. The reason for the lower rates, in our mind, in the neighboring States is clear competition.

These States either have access to other rail competition or to barge transportation. Since we are a State lacking competitive modes of transportation, and the fact that we are a major producer and shipper of raw bulk commodities, mainly coal, grain, and lumber, adequate and economical rail transportation is vital to keeping our products market competitive.

Montana's only other transportation alternative for bulk commodities is truck, which is substantially less efficient in the transportation of bulk commodities over long distances.

Average rail costs per net ton mile to move wheat from Montana to Pacific North Coast ports are 1.9 cents. Truck/barge movements average 3.25 cents per net ton mile.

The river transfer charge of $2.70 per ton is not included in the truck/barge costs, but would further increase these costs to make them even less competitive with rail movements.

The lowest truck/barge costs per net ton mile exceeds the highest Burlington Northern costs. The fact is that the truck/barge does not provide effective competition that would constrain rail rates.

The Burlington Northern far exceeds the 2,500 level of the Herfindahl-Hirschman Index which the U.S. Department of Justice uses to determine whether a company is in a monopoly position.

For Pacific Rim markets, the Index for Burlington Northern is 3,588 for Asia, and for the Pacific Rim, it is 2,652. We know that a financially healthy rail system is vital to our economy. We also understand that the Staggers Act is apparently working where intra- and intermodal competition exists.

We do not feel the ICC has properly interpreted and carried out the congressional intent of Staggers, particularly in areas pertaining to captive shippers, rate reasonableness, and determination of revenue adequacy.

While the antitrust concept of Senate bill 447 is not the total answer to our rail transportation problems, it would certainly help prevent monopoly pricing by railroads, and is a step forward in addressing the concerns of our shippers. Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF WILLIAM J. FOGARTY
ADMINISTRATOR, TRANSPORTATION DIVISION
MONTANA DEPARTMENT OF COMMERCE
SENATE COMMITTEE ON THE JUDICIARY
SEPTEMBER 24, 1985

Mr. Chairman, Members of the Committee, my name is Bill Fogarty. I am the Administrator of the Transportation Division, Montana Department of Commerce. I appreciate the opportunity to supply testimony in support of S.B. 447.

Montana's rail system consists of approximately 3,500 route miles of track operated primarily by three Class I Carriers (Burlington Northern Railroad, Soo and Union Pacific) and two recently-born short line carriers. Of this total, 825 miles are branch lines.

The dominant carrier is the Burlington Northern Railroad (BNRR) which operates over 91 percent of the route miles covering all portions of the state. The Burlington Northern serves 98 percent of the grain elevators in Montana and all the elevators with 26 and 52 car facilities with the exception of a 52 car facility at Butte on the Union Pacific System.

Since 1979, BNRR has abandoned 16 lines constituting a total of 400 route miles. Ten of these lines have been abandoned since 1983. In addition, the 66 mile Spring Creek Junction to Geraldine line was transferred to the newly created Central Montana Rail (CMR) short line as a result of a lawsuit settlement between the State of Montana and the BNRR.

An agreement consummated recently between the Butte, Anaconda & Pacific Railway Co. (BA&P) and the State of Montana resulted in the creation of RARUS, a new company that will operate a short line railroad in southwestern Montana, including over 43 miles of trackage previously served by the BA&P.

On their System Diagram Map, BNRR currently has one line in Category 1 (Railroad Preparing Abandonment Applications) constituting 28.5 route miles. Two lines are in Category 3 (Railroad Filed Abandonment Applications) constituting 15 miles.

The total number of miles abandoned by all carriers in the state since 1979 is 1,251 miles.

Besides the socioeconomic hardships caused to producers, shippers and businesses along the lost branch lines, the impacts on the areas' road systems caused by the diverted rail to truck traffic is devastating. On just one 66 mile branch line serving a grain area in central Montana, the state estimates the annual added highway impact costs to be at least $4.6 million.

From Exhibit I, the map of Montana's rail system, you will note that the BNRR trackage virtually blankets Montana, with the minor exceptions of the Soo Line in the extreme northeast corner and a Union Pacific branch line in the extreme southwest corner.

Upon comparing Montana's grain rates to states such as Colorado, Kansas, and Nebraska, our rates are consistently higher on a per car mile earning basis when comparing hauls of like commodities and distances. For example in Exhibit II attached, single car rates on a per car mile earnings in Montana, range from $ .48 to $1.60 per cwt higher. The increased revenues to BNRR from Montana's excessive rates on 26 car shipments range from $10,062 to $21,866 and to $25,480 to $45,760 for 52 car shipments.

In Montana, Burlington Northern's revenue to variable cost ratio on hard red wheat is 240 percent compared to BNRR's average earnings in other states on hard red wheat of 185 percent. Carriers other than Burlington Northern moving hard red wheat to the Pacific Northwest earn an average of 114.3 percent of revenue to variable cost. Let me clarify this with an example used by BNRR in the September, 1984 Senate Judiciary Committee Hearing. The BNRR grain rate from Omaha, Nebraska, to Pacific Northwest Ports and from Wolf Point, Montana, to Pacific Northwest Ports are as follows:

Wolf Point to Portland = 1,087 miles

Cars	Rate/Cwt	Loaded Revenue Per Ton Mile	Per Car Mile Earnings
52	161¢	.02962¢	$2.90

Omaha to Portland = 1,880 miles

Cars	Rate/Cwt	Loaded Revenue Per Ton Mile	Per Car Mile Earnings
54	154¢	.01638¢	$1.55

The facts show that BNRR's rate in Montana, is 4.5 percent higher than Omaha, but they earn 80.8 percent more per loaded ton mile and 86.6 percent more when put on a per car mile earnings basis out of Montana.

In 1981, the Montana grain producers filed a class action suit against the BNRR stating the grain rates in effect for the period of 1978-1980 were excessive. An ICC law judge in December, 1981 determined the BNRR did have market dominance in Montana, and that some rates were as high as 292 percent of revenue to variable costs. The BNRR then appealed the case to the full ICC. The ICC failed to make a decision on the case for approximately two years. In 1984, the ICC reopened the case saying market dominance and rate reasonableness had to be reproven under the definitions currently in place. The Montana grain producers have spent over $400,000 to cover expenses on the case thus far. The last Montana's legislative session approved an additional $310,000 for the state to assist in the case for the next two years. The ICC, through its delays and pro railroad bias, have done nothing to protect the captive shipper.

The reason for the lower rates in neighboring states is clear -- competition. These states either have access to other rail competition or barge transportation. Since we are a state lacking competitive modes of transportation and the fact that we are a major producer and shipper of raw bulk commodities, mainly coal, grain and lumber, adequate and economical rail transportation is vital to keeping our products market competitive.

Montana's only other transportation alternative for bulk commodities is truck, which is substantially less efficient in the transportation of bulk commodities over long distances.

Average rail costs per net ton mile to move wheat from Montana to Pacific North Coast are 1.9 cents. Truck/barge movements average 3.25 cents per net ton mile. The river transfer charge of $2.70/ton is not included in truck/barge costs, but would further increase these costs to make them even less competitive with rail movements. The lowest truck/barge costs per net ton mile exceeds the highest Burlington Northern costs. The fact is that the truck/barge does not provide effective competition that would constrain rail rates.

The Burlington Northern far exceeds the 2,500 level of Herfindahl-Hirschman Index which the U.S. Department of Justice uses to determine whether a company is in a monopoly position. For Pacific Rim markets, the Index for Burlington Northern is 3,588; for Asia and for the Pacific Rim it is 2,652.

We know that a financially healthy rail system is vital to our economy. We also understand that the Staggers Act is apparently working well where intra and intermodal competition exists. We do not feel the ICC has properly interpreted and carried out the congressional intent of Staggers, particularly in areas pertaining to captive shippers, rate reasonableness and determination of revenue adequacy. While the antitrust concept of S.B. 447 is not the sole answer to our rail transportation problems, it would help prevent monopoly pricing by railroads and is a step forward in addressing the concerns of captive shippers.

EXHIBIT #II

COMPARISON OF CAR MILE EARNINGS
REVENUE IN CENTS/CWT
FOR CARLOADS OF GRAIN
FROM MONTANA TO PORTLAND
VS
COLORADO, KANSAS, AND NEBRASKA TO HOUSTON

Montana Minimum Weight 196,000
CO, KS & NB Minimum Weight 190,000
Rate/Cwt
Single Car

Origin Points	Actual Miles	Rate Per CWT	Revenue/ Car[1]	PCME[2]
Meriwether MT	733	158¢	$3,097	$4.225
Fredonia KS	733	101¢	$1,919	$2.618
Difference	--	57¢	$1,178	$1.607
Townsend MT	785	152¢	$2,979	$3.795
Olathe KS	790	105¢	$1,995	$2.525
Difference	--	47¢	$ 984	$1.270
Joplin MT	833	162¢	$3,175	$3.812
Leavenworth KS	839	128¢	$2,432	$2.899
Difference	--	34¢	$ 743	$ .913
Kershaw MT	890	158¢	$3,097	$3.480
Lyons KS	896	104¢	$1,976	$2.205
Difference	--	54¢	$1,121	$1.275
Moccasin MT	938	163¢	$3,195	$3.406
Humbolt NE	946	138¢	$2,622	$2.772
Difference	--	25¢	$ 573	$ .634
Billings MT	987	163¢	$3,195	$3.237
Omaha NE	1005	138¢	$2,622	$2.609
Difference	--	25¢	$ 573	$ .628
Hardin MT	1045	174¢	$3,410	$3.263
Fremont NE	1047	138¢	$2,622	$2.504
Difference	--	36¢	$ 788	$ .759
Wolf Point MT	1087	196¢	$3,842	$3.535
Denver CO	1083	174¢	$3,306	$3.053
Difference	--	22¢	$ 536	$ .482
Culbertson MT	1141	196¢	$3,842	$3.367
Kearney NE	1147	161¢	$3,059	$2.667
Difference	--	35¢	$ 783	$ .700

[1] Rate x Minimum Weight = Revenue/Car
[2] Revenue/Car ÷ Actual Miles = Per Car Mile Earnings

EXHIBIT #II

COMPARISON OF CAR MILE EARNINGS
REVENUE IN CENTS/CWT
FOR CARLOADS OF GRAIN
FROM MONTANA TO PORTLAND
VS
COLORADO, KANSAS, AND NEBRASKA TO HOUSTON

Montana Minimum Weight 196,000
CO, KS & NB Minimum Weight 190,000
Rate/Cwt
26 Cars

Origin Points	Actual Miles	Rate/ CWT	Revenue/ Car[1]	PCME[2]	Earnings On 26 Cars[3]
Meriwether MT	733	135¢	$2,646	$3.610	$ 841
Fredonia KS	733	95¢	$1,805	$2.462	x 26
Difference	--	40¢	$ 841	$1.148	$21,866
Townsend MT	785	134¢	$2,626	$3.345	
Olathe KS	790	--	--	--	
Difference	--	--	--	--	
Joplin MT	833	138¢	$2,705	$3.247	$ 539
Leavenworth KS	839	114¢	$2,166	$2.582	x 26
Difference	--	24¢	$ 539	$ .665	$14,014
Kershaw MT	890	135¢	$2,646	$2.973	
Lyons KS	896	--	--	--	
Difference	--	--	--	--	
Moccasin MT	938	139¢	$2,724	$2.904	$ 387
Humbolt NE	946	123¢	$2,337	$2.470	x 26
Difference	--	16¢	$ 387	$ .434	$10,062
Billings MT	987	144¢	$2,822	$2.859	$ 485
Omaha NE	1005	123¢	$2,337	$2.325	x 26
Difference	--	21¢	$ 485	$ .534	$12,610
Hardon MT	1045	146¢	$2,862	$2.739	$ 525
Fremont NE	1047	123¢	$2,337	$2.232	x 26
Difference	--	23¢	$ 525	$ .507	$13,650
Wolf Point MT	1087	176¢	$3,450	$3.174	$ 391
Denver CO	1082	161¢	$3,059	$2.825	x 26
Difference	--	15¢	$ 391	$ .349	$10,166
Culbertson MT	1141	176¢	$3,450	$3.024	$ 695
Kearney NE	1147	145¢	$2,755	$2.402	x 26
Difference	--	31¢	$ 695	$ .622	$18,070

[1] Rate x Minimum Weight = Revenue/Car

[2] Revenue/Car ÷ Actual Miles = Per Car Mile Earnings

[3] Difference in Revenue/Car x No. of Cars in Shipment

EXHIBIT #II

COMPARISON OF CAR MILE EARNINGS
REVENUE IN CENTS/CWT
FOR CARLOADS OF GRAIN
FROM MONTANA TO PORTLAND
VS
COLORADO, KANSAS, AND NEBRASKA TO HOUSTON

Montana Minimum Weight 196,000
CO, KS & NB Minimum Weight 190,000
Rate/Cwt
52 Cars

Origin Points	Actual Miles	Rate/ CWT	Revenue/ Car[1]	PCME[2]	Earnings On 52 Cars[3]
Meriwether MT	733	120¢	$2,352	$3.209	$ 547
Fredonia KS	733	95¢	$1,805	$2.462	x 52
Difference	--	25¢	$ 547	$ .747	$28,444
Townsend MT	785	120¢	$2,352	$2.997	$ 490
Olathe KS	790	98¢	$1,862	$2.356	x 52
Difference	--	22¢	$ 490	$ .641	$25,480
Joplin MT	833	123¢	$2,411	$2.894	$ 549
Leavenworth KS	839	98¢	$1,862	$2.219	x 52
Difference	--	25¢	$ 549	$ .675	$28,548
Kershaw MT	890	120¢	$2,352	$2.643	$ 509
Lyons KS	896	97¢	$1,843	$2.057	x 52
Difference	--	23¢	$ 509	$ 586	$26,468
Moccasin MT	938	124¢	$2,430	$2.591	$ 416
Humbolt NE	946	106¢	$2,014	$2.129	x 52
Difference	--	18¢	$ 416	$ .462	$21,632
Billings MT	987	129¢	$2,528	$2.561	$ 514
Omaha NE	1005	106¢	$2,014	$2.004	x 52
Difference	--	23¢	$ 514	$ .557	$26,728
Hardon MT	1045	136¢	$2,662	$2.551	$ 652
Fremont NE	1047	106¢	$2,014	$1.924	x 52
Difference	--	30¢	$ 652	$ .627	$33,904
Wolf Point MT	1087	161¢	$3,156	$2.903	$ 420
Denver CO	1083	144¢	$2,736	$2.526	x 52
Difference	--	17¢	$ 420	$ .377	$21,840
Culbertson MT	1141	169¢	$3,312	$2.903	$ 880
Kearney NE	1147	128¢	$2,432	$2.120	x 52
Difference	--	41¢	$ 880	$ .783	$45,760

[1] Rate x Minimum Weight = Revenue/Car
[2] Revenue/Car ÷ Actual Miles = Per Car Mile Earnings
[3] Difference in Revenue/Car x No. of Cars in Shipment

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

Honorable Strom Thurmond
Chairman, Committee on the
  Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This letter expresses the views of the Department of Commerce on S. 447, the "Railroad Antimonopoly Act of 1985."

S. 447 is intended to protect captive rail shippers of bulk commodities. The bill amends the basic antitrust statute, the Sherman Act, to add provisions binding upon railroad carriers which operate "sole facilities." A sole facility is defined in the bill as a railroad facility which is the only facility by which a shipper can move bulk commodities to connect with a competing rail carrier.

Section 2 of the Sherman Act prohibits monopolization, attempts to monopolize, and agreements to monopolize. S. 447 adds to the Sherman Act a new definition of monopolization particular to railroads. The new section prohibits monopolization or attempts to monopolize defined as denying or threatening to deny a shipper or another rail carrier access and use of a sole facility on "reasonable terms." The bill describes two ways by which an owner of a sole facility may avoid violation. First, the carrier may rent use of its facility to a competing carrier on reasonable terms for track rental. Second, the carrier may charge rates "which are no higher than would yield a fair return on the proportion of the owner rail carrier's prudent investment in the sole railroad facility" as prorated to the traffic of the captive shipper. Finally, the bill provides for two types of relief. Injured persons may sue for treble damages under Section 4 of the Clayton Act or for injunctive relief under Section 16 of the Clayton Act. S. 447 removes the limitation of Section 16 that precludes suits against common carriers on any matter subject to the jurisdiction of the Interstate Commerce Commission.

The Department of Justice has testified in opposition to S. 447. Their opposition rested, in part, on their conclusion that the bill inappropriately grafts regulatory, industry-specific standards onto the antitrust laws. We object to the bill for that same reason.

In this Department's view, however, the complaints of shippers should be considered. President Reagan's National Coal Export Policy, issued July 18, 1981, assigned the Department of Commerce the lead role in coordinating Executive Branch efforts to reduce barriers to expansion of our nation's export coal trade. In light of this responsibility, as well as our Department's basic mission to "foster, promote and develop the foreign and domestic commerce of the United States," we have a significant interest in issues affecting captive shippers. Current conditions do not, in the Administration's view, merit legislative change. This Department will continue to listen to the complaints of export coal shippers.

We have been advised by the Office of Management and Budget that there is no objection to the submission of this report to the Congress from the standpoint of the Administration's program.

Sincerely,

Douglas A. Riggs

Senator **DeConcini**. Thank you. Mr. Chairman.

The **Chairman** [Mr. Thurmond presiding]. Mr. Bagalay, I believe you are next, are you?

Mr. **Bagalay**. Yes, sir.

The **Chairman**. I might say, too, that I have a statement. I think it has been turned over to the reporter just after the opening of the session.

Mr. Bagalay, you may proceed.

STATEMENT OF JOHN BAGALAY

Mr. **Bagalay**. I am the general counsel of the Lower Colorado River Authority which is an independent State agency. We provide, among other things, electric power and energy to 41 counties in central Texas, which includes about 30 municipalities, 11 rural electric cooperatives, and 4 cities which we serve directly.

And that covers about 1 million people, or just slightly less. We are not a monopoly. We do not operate with a franchise. We have no protected service area.

The only thing that we have to offer the public and our customers is competitive pricing in electric energy. Our experience in terms of fulfilling that obligation to offer the cheapest electrical utility prices that we can, is in part directly dependent upon the cost of transportation.

As one of the few independent State agencies subject to public utility regulation in this country, our fuel cost factor, which includes the transportation charge, is passed directly to the consumer. We were able, by moving from a "captive shipper" situation in Montana to a competitive transportation situation in Wyoming, to reduce the cost per ton of our coal which constitutes about 65 percent of our fuel, from $27.41 a ton to $22 a ton, simply because we found two railroads in dialog with each other, and with us.

Now that resulted in about a $20 million annual reduction in the cost, which flowed absolutely, directly to the consumer.

There are obviously many ways that one can approach the question of competition in the United States. Regulation is one and antitrust is another.

My own belief is that both have served us well, but perhaps the most direct empirical evidence which we at the LCRA have had, is the introduction of competition, because then the railroads started talking to us in a direct dialog.

I would suggest that the railroads' interest in competing for this business demonstrates their capacity to and willingness to survive in a competitive environment.

The cities of San Antonio, Houston, Austin and the LCRA were the pleasant beneficiaries of serious efforts on the part of competing railroads to get our business, and we suggest that both the consumer and the railroads, and the public, can survive in a competitive environment, and we urge the Senate and the Congress of the United States to address this very important question which deals directly with the electric utility companies and with the consumer. Thank you.

[The statement follows:]

AMERICAN PUBLIC POWER ASSOCIATION
2301 M STREET NW WASHINGTON DC 20037 • 202/775-8300

STATEMENT OF

John Bagalay
General Counsel
Lower Colorado River Authority

on

THE RAILROAD ANTIMONOPOLY ACT

Mr. Chairman, members of the Subcommittee, my name is John Bagalay. I am General Counsel of the Lower Colorado River Authority (LCRA), a conservation and reclamation district created by the Texas Legislature in 1934. LCRA is authorized to develop, generate, distribute and sell hydroelectric and thermalelectric power within a 41 county area of central Texas. LCRA sells electricity at wholesale to 30 municipal utilities and 11 rural electric cooperatives and at retail in 4 municipalities.

I am testifying on behalf of LCRA and the American Public Power Association (APPA), a national service organization representing approximately 1,750 municipal and other local publicly owned electric systems throughout the country.

Because many of APPA's members rely on coal to generate electricity, APPA has a vital interest in matters affecting the rail transportation of coal. We appreciate the opportunity to appear before you this morning and applaud the Committee's interest in examining the antitrust approach as a solution to the problems of captive coal shippers. As the appended policy resolution makes clear, APPA endorses S. 447, the Railroad Antimonopoly Act of 1985, as "an effective means for ensuring the benefits of competitive pricing in rail transportation."

THE LCRA STORY

In 1961 LCRA's electric generation was 100 percent dependent upon falling water. Today, hydro provides only 4.2 percent of the system's 1830 megawatts of generating capacity, with 32.5 percent provided by natural gas and 63.3 percent provided by coal.

LCRA is a partner with the city of Austin in the Fayette Power Project, a two-unit power plant that requires 4 million tons of coal per year. The coal is hauled by rail approximately 1500 miles from sources in the Powder River Basin, with the primary carrier being the Burlington Northern. LCRA owns ten unit trains as well as a shop for major maintenance on the equipment. The railroad provides the track, some switching and the power to pull the train.

Despite the "no frills" services, LCRA's rail rates have risen steadily in recent years. In November, 1978, the rates were $16.17 per ton. By July, 1984, the rates had climbed to $27.67 per ton from Montana sources (a 71 percent increase) and to $26.70 per ton from Wyoming (a 65 percent increase). Over that period of time there were 24 separate rate increases.

With the opening of the Chicago and North Western line into the Powder River Basin, competition has begun to lower the monopoly rates the BN has enjoyed. On April 1, new short-term contracts went into effect with two primary carriers that lowered the Wyoming rate from $26.70 to $22 per ton while the rate for Montana, served by a single carrier, was reduced almost $2 per ton. In addition, the new agreements resulted in improved turn-around time by approximately fifty-hours and thus enabled us to give up two leased trains. We are continuing to negotiate with both the BN and the CNW, and we are hopeful that this will result in even greater reductions in rail rates in the future.

Despite the increased competition, our experience with Burlington Northern has caused LCRA to make substantial changes in our fuel supply plans for the future. To lessen our dependency upon the railroads we are planning for the third solid fuel unit, Fayette Power Project III, which will come on line in January, 1988, to be fired by Texas lignite. This was not an easy decision, for it moves LCRA into a new line of business -- lignite mining -- and involves us with a fuel which requires more careful anti-pollution planning and controls. But those caveats were more than counterbalanced by the wisdom of diversifying our fuel sources, developing a Texas fuel with substantial reserves, and more than anything, lessening our dependency on the railroads.

COAL, RAILROADS AND THE ELECTRIC UTILITY INDUSTRY

Over the last decade national energy policy has sought to encourage the use of coal, an abundant domestic resource, in place of petroleum. This policy has been a significant success thus far. Since 1973, 80 percent of the increase in utility generating capacity has been coal-fired. Coal has risen from 42 percent of total generation to 53 percent. The result has been a reduction in oil-fired generation of more than one million barrels per day.

That trend is now threatened, however, by the monopoly profits that are being imposed upon captive coal shippers by America's railroads. Sixty percent of utility coal is delivered by rail, and approximately 85 percent of that rail-shipper utility coal is captive to one railroad.

Railroads have not hesitated to take advantage of the vulnerability of captive shippers. In 1981, according to the latest data from the Interstate

Commerce Commission, coal contributed over one-third of the railroads' gross operating profit. In fact, coal enjoys the highest profit margin of any commodity shipped by rail.

The reasons for such high profits are evident from a close look at the industry -- increased coal traffic, increased efficiency, and effective use of monopoly power. From 1976 to 1984 coal traffic rose from 405 million tons to over 500 million tons (estimate) or from 26 to 38 percent of total rail traffic. In addition, length of hall over that time has also increased by almost 60 percent. Much increased efficiency in coal hauling is due to utility investments, whether in efficient terminal loading and unloading facilities or through unit trains. Utilities have invested over $1.25 billion in coal cars, and half of all coal transported by rail is now moved in utility or producer-owned cars. Such efficiencies in coal movement have led to ton-mile costs that average 43 percent of other traffic.

As costs have decreased and profits have soared, however, rail coal rates have continued to climb, increasing 39 percent in constant dollars since 1976. According to Dr. Mark Cooper of the Consumer Federation of America railroads are now extracting monopoly profits of $1.3 billion annually from coal shippers and electricity consumers.

These monopoly profits are in too many instances not being reinvested in the rail industry but are instead funding a massive acquisition campaign by the coal hauling railroads. For example, in 1981-82 the Burlington Northern purchased El Paso Natural Gas Company for $1.3 billion. CSX bought Texas Gas Resources in 1983 for a billion dollars and last year purchased the nation's largest barge line, American Barge Lines. Norfolk Southern likewise recently purchased North American Van Lines and is striving to take over Conrail for $1.2 billion.

These three railroads -- the Burlington Northern, CSX, and Norfolk Southern -- haul 75 percent of the coal which is moved by rail. Despite their acquisitions and other strong indicators of financial health the ICC continues to find them "revenue inadequate." However, when vast accumulations of capital are obtained through differential pricing, allowed only in consideration of the railroads' claims of desperate need, it is time for the ICC to ask: How is it that allegedly revenue-inadequate railroads -- which are allowed rate increases that are not cost-based -- happen to have resources of a magnitude that permit them to buy a series of billion dollar corporations? We contend that it was not the purpose of the Staggers Act to allow coal rates so high that such acquisitions could be financed through monopoly profits imposed upon captive shippers.

THE ICC AND IMPLEMENTATION OF THE STAGGERS ACT

The extensive market power which the railroads presently possess over the preponderance of utility coal movements makes these receivers particularly susceptible to supra-competitive rail rates, market abusive service rules and practices, and other dysfunctional consequences of efforts to increase railroad profits at the expense of utility ratepayers. Under the Interstate Commerce Act, these captive shippers ostensibly are given statutory protection from unreasonable rates and practices -- the "flip-side" of the compromise in 1980 which also freed the railroads from most regulatory burdens in competitive markets. Unfortunately, implementation and application of the Act by the Interstate Commerce Commission has completely deprived monopolized shippers of the protections Congress intended them to have. The end result has been the de facto repeal -- through non-enforcement -- of many relief provisions, and the over-expansion of those provisions granting freedom or flexibility to rail carriers in markets which they dominate.

In both individual cases and general rulemaking proceedings, the ICC has shown a one-dimensional dedication to increased rail freight revenues, and has ignored Congress' direction that the ICC balance the needs of shippers, carriers and the general public. A brief review of its resolution of certain key issues is illustrative.

Revenue Adequacy

"Adequate" revenues were defined by Congress as a level of earnings sufficient to enable a carrier to meet all of its expenses, retire a reasonable amount of debt, cover planned depreciation and obsolescence, and earn a return on investment sufficient to attract new capital. Through a combination of rate flexibility, increased operating efficiency, and plant streamlining and modernization, carriers were to be assisted in attaining the goal of revenue adequacy. To this end, revenue adequacy was to be considered as one of several factors in railroad ratemaking cases.

Under the ICC's interpretation, both the definition and role of revenue adequacy as established by Congress have been completely transformed. No longer a synonym for "financial health," it has been redefined by the ICC as an almost magical level of earnings which would be realistically unattainable in virtually any industry. It is now the Commission's lodestar for rail carrier rate freedoms -- in practical terms the only ratemaking goal the Commission now recognizes -- and has been so misshapen as to bear little resemblance to credible indicia of financial health used throughout the financial community. In addition, it produces results wholly at odds with reality: The billion dollar cash acquisitions I mentioned earlier, especially the Norfolk Southern touting its financial health while offering $1.2 billion in cash for Conrail, all juxtaposed against the fact that all major coal hauling railroads are considered "revenue inadequate" to the tune of several hundred million dollars each by the ICC.

Maximum Rate Regulation

After wrestling for many years with the question of the maximum levels at which railroad rates on captive traffic -- especially coal traffic -- should be set, the ICC has now abdicated its responsibility to regulate rates in market dominant situations by devising a set of guidelines which would allow monopoly railroads to charge any rates they desire on captive coal traffic so long as the rate does not exceed the shipper's cost of owning and operating its own railroad. As interpreted by the railroad industry in individual cases, this standard would permit rates in excess of 500 percent of the railroads' cost of service.

Moreover, in conflict with the clear intent of Congress in 1980, the Commission's proposed guidelines sanction the railroads' looking exclusively to captive coal traffic for full recovery of their perceived revenue shortfalls. This is apparent from the fact that the Commission developed a rate increase "phase-in" by measuring the amount of time it would take the nation's carriers to achieve "revenue adequacy" (as defined by the ICC) through the application of annual rate increases exclusively on utility and other captive coal traffic. Many coal rates can increase dramatically under the guidelines -- which recently received formal Commission approval and should be released in final written form any day now -- with the attendant transfer of billions of dollars from the nation's utility ratepayers to the railroads. Once implemented with respect to coal traffic, it is expected that these guidelines also will be applied in all cases involving captive commodities.

Market Dominance

As designed by Congress, the statutory concept of "market dominance" was to provide a mechanism for timely threshold determinations of whether a given shipper's traffic was exposed to rail market power and thus qualified for ICC rate review. The Commission's current guidelines for implementing this concept, however, which have gone through several mutations since its original enactment in 1976, require shippers to engage in complex, protracted and expensive antitrust-type proceedings simply to establish ICC jurisdiction to examine the reasonableness of a rail rate. Originally, market dominance determinations were to be made within ninety days. One recent case under the Commission's guidelines, however, took four years to reach a resolution on the issue of market dominance alone. Multiple expert witnesses, hundreds of interrogatories and document production requests, and thousands of pages of record evidence are now typically devoted to what originally was intended to simply be a threshold determination of jurisdiction. Predictably, the problem has begun to take on Kafkaesque attributes: one shipper recently spent more than its entire annual rail freight bill simply to demonstrate to the ICC that it was entitled to challenge those very rates under the maximum rate standards of the Interstate Commerce Act.

The Commission has also consistently expanded the scope of the term "market dominance," and went to ridiculous lengths in a recent decision to rule against a market dominance finding. In a complaint brought by APPA member Salt River Power District against the Atchison, Topeka & Sante Fe Railway, the ICC declared that the utility had "flexibility in determining how much power it will produce and at which plants," which supposedly added to SRP's leverage to prevent excessive rates.

State-Federal Relations

Seeking a degree of uniformity of treatment, the Staggers Act modified the way in which individual states regulate intrastate rail transportation. States must now do so by applying the "standards and procedures" of the Interstate Commerce Act, and the ICC may set aside state agency decisions only if it determines that the standards and procedures applied by the state were not in accordance with Federal law.

The ICC has interpreted the scope of its review authority as allowing it to set aside any state decision which does not contain a result identical to that which the ICC would have reached. Since the ICC has yet to hold down a rail rate increase on coal traffic, the predictable result has been that each state agency decision which has disallowed all or part of a rate increase sought by a railroad has been set aside. In each case, the rate increase sought by the carriers has been approved by the ICC. The same pattern is following when states seek to exercise their regulatory jurisdiction to promote or enhance competition, suspend the implementation of inequitable carrier service practices, or otherwise respond to formal shipper complaints.

Competitive Access Issues

Expanded carrier authority under the Staggers Act to re-arrange joint rate and route relationships and reciprocal switching arrangements was intended to permit the railroads to rationalize their plant investment, increase operational efficiency, and promote competition. With the blessing of the ICC, however, many carriers have used these new freedoms to foreclose competition, divide markets and retaliate against small or regional railroads that resist the major carriers' pricing aspirations. This problem is particularly acute in the East, where Conrail's efforts to compete in the export coal market were met by CSX-sponsored joint rate cancellations and route closings, and where many shippers who had previously enjoyed access to a number of different carriers or modes now find themselves captive to a single railroad that has succeeded in manipulating its power under the Commission's laissez-faire view of regulatory policy to squeeze out the competition.

There are a number of other, less notorious examples of the ICC's mal- and non-feasance in the area of captive shipper protections, which only serve to exacerbate the inequitable situation resulting from the actions I have just described. In the final analysis, all of these developments point to a prevailing view on the part of the ICC that the only real goal of the Staggers Act was to increase the revenues of major rail carriers, and that any action which fosters this goal deserves pre-eminence. Today, the Commission views those provisions of the Interstate Commerce Act which are designed to preserve competition and restrain rates on captive rail traffic as hurdles to be overcome, rather than substantive policy to be enforced.

Meaningful change in the status quo is necessary, and it is Congress that must bring about that change. The ability of the courts to modify the Commission's misguided constructions and applications is limited, and efforts by shippers and other interested parties to seek reform through the administrative process largely have fallen on deaf ears. I agree that as a rule, legislation should be a last resort to commercial or economic problems. In the case of effective protections for captive rail shippers, however, we have reached the end of the line and have no alternative. Through one means or another, Congress must act to restore effectively the balance between shipper and carrier interests which it sought to strike in 1980.

THE RAILROAD ANTI-MONOPOLY ACT OF 1985

There are only two possible responses that will protect the public from the high rates and inefficient service that seem to inevitably accompany unfettered monopoly. The first is effective regulation to protect captive shippers, which is the objective of the Consumer Rail Equity Act, S. 477. Both LCRA and APPA are active members of Consumers United for Rail Equity (CURE), the coalition which is working on behalf of S. 477. Without such a reaffirmation of Congressional intent it is doubtful that the Interstate Commerce Commission will move any closer toward an evenhanded implementation of the Staggers Act.

The second option available to Congress is to take steps to expand competition to monopoly situations. With the deregulaton of competitive rail traffic, the ICC's refusal to use the authority it has to regulate captive traffic, and an increasingly concentrated industry, it makes eminent sense to extend the antitrust laws to the railroad industry so as to encourage competition and protect against monopoly abuse. That is the intent of S. 447, the Railroad Antimonopoly Act of 1985, a bill which APPA has formally endorsed as "an effective means for ensuring the benefits of competitive pricing in rail transportation." We commend Senator DeConcini for his efforts in support of the bill. We view the antitrust approach in S. 447 as compatible with the "improved regulation" approach of the CURE bill and feel that both should be supported by shippers and consumers as complementory means to achieving reasonable rates.

S. 447 attempts to make a correction which has been made necessary by the historical evolution of the law. In the early part of this century the Supreme Court held that the Sherman Act could be applied to protect against railroad abuse of monopoly power. But the 1922 Keough decision protected railroads from antitrust damage awards because of the regulatory jurisdiction of the ICC. In addition, section 16 of the Clayton Act specifically shields railroads from antitrust injunction actions by private parties.

The railroads now have the best of both worlds -- an irresponsible regulatory agency that refuses to implement the law as Congress intended along with almost total immunity from the antitrust laws. The industry cannot continue to have it both ways. In exchange for the benefits of deregulation being extended to their competitive traffic it is reasonable to expect the now outdated immunity from antitrust action would be lifted.

S. 447 is a fitting vehicle through which to achieve that objective. Despite the protestations of the railroads, S. 447 is a moderate and relatively narrowly drawn bill which simply extends the essential facilities doctrine to the railroad industry and overturns some of the limits imposed by the Keough decision. The bill would apply to a rail facility which is the sole facility over which a shipper can connect by rail with track of a competing railroad for the final destination. It would require the monopoly rail carrier to either (1) open the use of its sole facility to competition by another railroad for reasonable terms or (2) offer reasonable rates to the shipper for use of the sole facility which do not provide monopoly profits.

LCRA is all too familiar with the plight of the captive shipper, and yet we also have first hand experience with the power of competition in the rail industry. When the Chicago and North Western opened its line into the Powder River Basin LCRA and other captive shippers saw their rates decrease by between 15 and 29 percent.

Unfortunately, the rail industry is growing increasingly concentrated. As joint rates and route agreements are cancelled left and right the industry is moving more toward monopoly than increased competition. S. 447 could be an important tool to assist in opening the industry to greater competition, providing leverage to captive shippers to negotiate more reasonable rates.

We commend the Committee for initiating these hearings, and urge your favorable action on the legislation.

AMERICAN PUBLIC POWER ASSOCIATION
2301 M STREET NW WASHINGTON DC 20037 • 202/775-8300

"TRACKAGE RIGHTS" FOR CAPTIVE RAIL SHIPPERS

WHEREAS, because 52 percent of electric generation in the United States today is fueled by coal, and 85 percent of all coal shipped by rail is captive to one railroad, the price of electricity is greatly influenced by the costs of rail transportation charged to captive coal shippers, and

WHEREAS, the rate deregulation provisions of the Staggers Rail Act of 1980 were premised on the belief that market competition exists in significant measure and would restrain excessive price increases in large segments of the railroad industry, but this belief is clearly unfounded in many regions, and

WHEREAS, since the enactment of the Staggers Rail Act of 1980, the Interstate Commerce Commission has interpreted the Act in a manner designed to grant railroads virtually unlimited pricing freedom for transporting coal and other captive commodities, despite the Act's intent to continue rail rate regulation where railroads possess monopoly power, and

WHEREAS, in 1983, the American Public Power Association called for legislation to amend the Staggers Rail Act to strengthen essential regulatory protection for captive shippers from monopolistic pricing practices, and

WHEREAS, increased competition in rail services, in addition to effective rate regulation, would greatly benefit captive shippers and consumers through marketplace price discipline, and

WHEREAS, Representative John Seiberling (D-OH) and Senators Dennis DeConcini (D-AZ) and Max Baucus (D-MT) have introduced legislation (H.R. 4559 and S. 2417) to increase rail industry competition by amending the Sherman Antitrust Act to make it unlawful for a rail carrier to deny to any shipper the use of a rail facility which is the sole means by which the shipper can connect by rail with the trackage of a competing rail carrier or reach the destination of a shipment, if such denial is with the intent to monopolize;

NOW, THEREFORE, BE IT RESOLVED: that the American Public Power Association endorses H.R. 4559, the Electric Consumers' Railroad Antimonopoly Act, and S. 2417, the Consumers Railroad Transportation Antimonopoly Act, as effective means for ensuring the benefits of competitive pricing in rail transportation, and also reaffirms its support for legislation to strengthen shipper protections from monopolistic pricing through effective regulation, where railroads continue to exercise monopoly power over the freight transportation of coal and other commodities.

-- Adopted June 12 by the membership of the American Public Power Association at its 1984 Annual Conference in Boston, Massachusetts.

Lower Colorado River Authority
Post Office Box 220 Austin, Texas 78767 AC 512 473-3200
JOHN E. BAGALAY, JR., General Counsel • 473-3238

September 30, 1985

The Honorable Charles E. Grassley
United States Senate
Washington, D.C. 20515

RE: S.477, The Railroad Antimonopoly Act of 1985

Dear Senator Grassley:

During the hearing held on the referenced legislation on September 24, 1985, you asked witnesses testifying on behalf of rail shippers whether the Interstate Commerce Commission's actions in the proceeding docketed as Ex Parte No. 456, Staggers Rail Act of 1980 -- Conference of Interested Parties addressed in a positive way the captive shipper problems to which the Railroad Antimonopoly Act is addressed. The purpose of this letter is to supplement my oral response to your inquiry, and I would request that it be included in the final hearing record.

The Commission's Ex Parte No. 456 process resulted in the institution of two new proceedings, denominated Ex Parte No. 320 (Sub-No. 3) and Ex Parte No. 445 (Sub-No. 1). The first proceeding addressed and ultimately adopted a negotiated proposal presented jointly by the Association of American Railroads, the American Paper Institute and the National Industrial Transportation League to modify slightly the standards applied by the Commission in making jurisdictional determinations of rail market dominance under 49 U.S.C. §10709. In Ex Parte No. 445 (Sub-No. 1), the Commission voted to adopt new procedures of the Interstate Commerce Act dealing with joint rates and through routes (49 U.S.C. §10705a) and reciprocal switching arrangements (49 U.S.C. §11103(c)). These procedures, which also are based on a negotiated settlement between AAR and NITL, ostensibly are intended to address more effectively problems of so-called "competitive access" to captive shippers and markets. Both the market dominance and the competitive access proposals appear to be well-intentioned, and may represent a modest improvement in the *status quo*, but neither addresses the captive shipper problem effectively so as to reduce the need for legislative action.

The new market dominance guidelines (Ex Parte No. 320 (Sub-No. 3)) make certain changes in allocations of the burden of persuasion as between a shipper challenging a railroad rate and the carrier defendant(s), but they otherwise fail meaningfully to improve upon the byzantine market dominance guidelines now applied by the Commission, under which threshold determinations of jurisdiction are converted into complex, antitrust-type litigation, and findings which Congress intended to be made within 90 days can take -- as one recent case demonstrated -- up to four years to complete. In addition, the "new" guidelines continue to sanction consideration of potential geographic and product competition in determining whether a shipper is effectively captive to the railroad(s) charging the challenged rates. Consideration of these factors will continue to permit findings of no market dominance -- and thus no right on the shipper's part to seek a determination of rate reasonableness -- even though the source of alleged "competition" is only potential, and would not, even if it materialized, enable the shipper to shift all or even a majority of the traffic subject to the challenged rate to an alternative carrier or mode.

Not only do the Ex Parte No. 320 (Sub-No. 3) guidelines fail to arrest the trend toward a narrowing of shippers' rights to challenge the reasonableness of rail rates, they do nothing whatsoever to rectify the principal roadblock to effective rate relief for coal shippers: the Commission's "anything goes" policy toward determinations of maximum reasonable rates on coal. As Congress has repeatedly heard through hearing testimony, and as recently confirmed by the Commission's September 3, 1985 decision in Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines -- Nationwide, the ICC's announced coal rate policy will permit a carrier to charge any rate it chooses on captive coal traffic, so long as the carrier remains "revenue inadequate" as defined by the ICC and the rate is not higher than the shipper's cost of building and operating its own railroad. The problem of an absence of meaningful regulatory restraint on captive coal rates, a principal motivating force behind the Railroad Antimonopoly Act, thus remains, Ex Parte No. 320 (Sub-No. 3) notwithstanding.

The situation is much the same with regard to Ex Parte No. 445 (Sub-No. 1), the so-called "competitive access" rules. While the Commission proposes to tinker somewhat with the notice requirements and evidentiary guidelines incident to efforts by rail carriers to cancel joint rates or close through routes, the AAR/NITL compromise offers little in the way of an expansion of the Commission's exercise of its authority to order reciprocal switching where necessary to enhance rail competition. Moreover, those rules do not address at all the subject of terminal trackage rights, the aspect of existing law (49 U.S.C. §11103(a)) that bears the closest relationship to the central thesis of the Railroad Antimonopoly Act. With regard to the initiation of new competition in captive markets, therefore, the advocates of the Ex Parte No. 445 (Sub-No. 1) proposal and the Commission are prepared to accept "business as usual" with no meaningful changes.

Such an attitude offers nothing of value to captive coal and other bulk commodity shippers, since under the status quo the Commission has been steadfast in its refusal to use its power under 49 U.S.C. §11103 actively to pursue an expansion of competition in markets dominated by individual railroads. This attitude is most recently exemplified by the July 15, 1985 Commission decision in Midtec Paper Corporation v. Chicago and Northwestern Transportation Company. In that case, the Commission denied relief to a shipper under §11103, ruling that a shipper seeking reciprocal switching or trackage rights in order to generate competition and reduce its rail rates effectively must first show that those rates are unreasonably high under the Interstate Commerce Act. In grafting this requirement -- as well as the jurisdictional requirement of a showing of market dominance -- onto the statutory standards of §11103, the Commission has gone well beyond the letter and intent of Congress in this area, and quite possibly may have put the pro-competitive remedies of that section out of reach of individual shippers, if the laissez-faire approach to rate reasonableness adopted with respect to coal is expanded to other captive commodities as well.

Far from obviating the need for legislative action, the Commission's unwarranted narrowing of the availability of trackage rights and reciprocal switching in the Midtec case demonstrates that regardless of rhetoric surrounding the "competitive access" guidelines of Ex Parte No. 445 (Sub-No. 1), the Commission either does not believe that it possesses the statutory authority to address the problems of captive shippers by working to bring effective competition into new areas, or is unwilling to use the power it does have toward that end. In either case, the Commission's current approach to the matter of competitive access leaves much to be desired, and provides ample evidence of the need for legislative intervention in this area.

I appreciated the opportunity to appear before the Committee to address some of the important issues surrounding this legislation, and I hope that this letter significantly augments my oral statement in response to your question concerning current ICC policies. Should you or a member of your staff have any additional questions regarding my testimony or LCRA/Austin's experience in connection with competitive coal transportation, please do not hesitate to contact me.

Very truly yours,

Jon E Bagalay, Jr.

krs

cc: The Hon. Strom Thurmond
Chairman
Senate Committee on the
Judiciary

The Hon. Edward M. Kennedy
Ranking Minority Member

Senator DECONCINI [presiding]. Mr. Bagalay, thank you. Mr. Yager.

Mr. JOHNSTON. Mr. Chairman, I am Don Johnston.

Senator DECONCINI. All right, Mr. Johnston, we will hear you.

STATEMENT OF DON M. JOHNSTON

Mr. JOHNSTON. Yes. Mr. Chairman, in the essence of time, I would be happy to submit my testimony for review by the Committee, but briefly, would introduce myself by telling you that I am a farmer, grower, packer, shipper, from Kern County, CA, and I am on the board of directors of the United Fresh Fruit & Vegetable Association and am representing that group today.

I am also chairman of the Western Growers Association Transportation Committee. United represents approximately 80 percent of the perishable commodities shipped within the United States.

I have experienced, firsthand, considerable and numerable problems existing in single line rail usage, and am happy to submit my testimony and respond to any questions that the Committee may have.

I have also brought with me today Mr. Dickson Loos, legal counsel of United Fresh Fruit Vegetable Association.

[The statement follows:]

STATEMENT OF
DON M. JOHNSTON
MEMBER, BOARD OF DIRECTORS
UNITED FRESH FRUIT AND VEGETABLE ASSOCIATION

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE, MY NAME IS DON M. JOHNSTON OF JOHNSTONFARMS IN EDISON, CALIFORNIA. I AM APPEARING HERE TODAY AS A GROWER, PACKER AND SHIPPER OF CALIFORNIA ORANGES AND POTATOES, AND AS A MEMBER OF THE UNITED FRESH FRUIT AND VEGETABLE ASSOCIATION. FURTHERMORE, I CURRENTLY SERVE AS A MEMBER OF THE BOARD OF DIRECTORS OF UNITED, THE NATIONAL TRADE ASSOCIATION OF THE FRESH FRUIT AND VEGETABLE INDUSTRY. UNITED REPRESENTS 2,500 MEMBER COMPANIES AND ORGANIZATIONS THROUGHOUT THE UNITED STATES AND IN 21 COUNTRIES. THE MEMBERSHIP IS INVOLVED IN ALL FACETS OF THE FRESH PRODUCE INDUSTRY, INCLUDING GROWING, PACKING, SHIPPING, WHOLESALING AND RETAILING FRESH PRODUCE TO AMERICAN CONSUMERS. UNITED'S MEMBERS HANDLE OVER 80 PERCENT OF ALL FRESH PRODUCE MARKETED COMMERCIALLY IN THE UNITED STATES.

IT IS A PLEASURE FOR ME TO TESTIFY BEFORE YOUR DISTINGUISHED COMMITTEE ON S. 447, THE RAILROAD ANTIMONOPOLY ACT. WHILE I AM NOT A LEGAL SCHOLAR OR AN ANTITRUST ATTORNEY, I AM A PRACTICING FARMER WITH FIRST HAND KNOWLEDGE OF HOW FARMERS WITH PERISHABLE COMMODITIES HAVE, TO DEAL WITH THE RAILROADS. I HOPE TODAY I CAN SHARE WITH YOU SOME ACTUAL RAIL PROBLEMS AND SPECIFIC OUTRAGEOUS RAIL PRICING EXAMPLES THAT HIGHLIGHT WHY OUR INDUSTRY SUPPORTS S. 447.

LET ME FIRST MAKE IT VERY CLEAR THAT UNITED AND ITS MEMBERS DO NOT FAVOR A RETURN TO GOVERNMENT REGULATION OF THE RAIL INDUSTRY. AS YOU MAY KNOW, THE PERISHABLE INDUSTRY SUPPORTED DEREGULATION AND OUR INDUSTRY HAS BEEN DEREGULATED FROM ICC ECONOMIC REGULATION SINCE 1979. WE SUPPORTED THIS ACTION HOPING THE FUTURE WOULD PERMIT THE RAILROADS TO MAXIMIZE THEIR OPERATIONAL EFFICIENCIES. LIKE ANY INDUSTRY THAT DEPENDS ON RAIL TRANSPORTATION, WE WERE CONCERNED ABOUT THE FINANCIAL SURVIVABILITY OF THE RAIL INDUSTRY AND SOUGHT FINANCIALLY STRONG RAILROADS THAT COULD MAINTAIN AND IMPROVE THE PHYSICAL QUALITIES OF OUR NATION'S RAIL SYSTEM.

HOWEVER, THE RESULT HAS BEEN DICTATORIAL RAILROAD POLICIES BY GIANT RAILROADS. INSTEAD OF INCREASED COMPETITION FOR RAIL BUSINESS, WE HAVE WITNESSED UNPRECEDENTED RAILROAD MERGERS, LEAVING LARGE SEGMENT OF THE COUNTRY TO BE SERVICED BY ONLY ONE RAILROAD.

LET ME SHARE WITH YOU SOME EXAMPLES:

IN THE LUSH GROWING AREAS OF KERN COUNTY, CALIFORNIA, WERE I LIVE AND FARM, POTATO GROWERS AND SHIPPERS, IN THE PEAK OF OUR HARVEST LAST JUNE, WERE CONFRONTED WITH UNCONSCIONABLE RAIL SHIPPING RATES. UNDER THE HEAT OF 110 DEGREE TEMPERATURES, THE SOUTHERN PACIFIC RAILROAD INCREASED RAIL RATES OF MECHANICAL REFRIGERATED BOXCARS BY OVER $600 PER WEEK FOR THREE WEEKS. SOUTHERN PACIFIC CARLOAD RATES FOR POTATOES SHIPPED FROM CALIFORNIA TO CONSUMERS IN BOSTON INCREASED FROM $6,960 ON MAY 27 TO $9,860 ON JUNE 17. DURING THE SAME PERIOD, RATES FOR IDAHO POTATOES TRAVELING A SIMILAR DISTANCE ON THE UNION PACIFIC RAILROAD REMAINED A CONSTANT $5,750. A DIFFERENCE OF $4,110 PER CARLOAD!

POTATO GROWERS ARE BULK CAPTIVE SHIPPERS SINCE THE VOLUME, COMMODITY WEIGHT AND DISTANCE OF HAUL ARE ADOPTABLE ONLY TO THE ECONOMIES AND EFFICIENCIES OF RAIL TRANSPORTATION. TRUCKS, AT MOST ANY PRICE, COULD NOT EVEN MAKE A RESPECTABLE DENT IN OUR TRANSPORTATION NEEDS. NO SINGLE CORPORATION OR MAJOR AMERICAN INDUSTRY SHOULD BE ABLE TO DICTATE THIS TYPE OF PRICING PRACTICES THAT LITERALLY ARE PLACING SMALL FARMERS AND A ONCE PROSPEROUS FARMING INDUSTRY IN CALIFORNIA OUT OF BUSINESS.

IN ANOTHER WEST COAST EXAMPLE, THE SOUTHERN PACIFIC HAS THREATENED A NUMBER OF TIMES TO CUT OFF SERVICE TO A NUMBER OF CAPTIVE SHIPPERS IF THEY DID NOT AGREE TO NEW MASTER TRANSPORTATION AGREEMENTS, WRITTEN IN THEIR CORPORATE OFFICES WITHOUT THE BENEFIT OF MEANINGFUL DISCUSSIONS AND NEGOTIATIONS WITH SHIPPERS.

SPECIFICALLY, IN NOVEMBER OF 1984, THE SOUTHERN PACIFIC NOTIFIED PACKING HOUSES OF SUNKIST GROWERS THAT THEY WERE CUTTING OFF THEIR SERVICE THE NEXT MORNING BECAUSE SUNKIST REFUSED TO AGREE TO THE SOUTHERN PACIFIC'S NEW TRANSPORTATION AGREEMENT. INCLUDED IN THE "ONE-WAY" AGREEMENT, WAS A PROVISION THAT PERMITTED THE RAILROAD TO CHARGE A SHIPPER TWO DAYS DETENTION AND DEMURRAGE IF THE SHIPPER USED A BOXCAR SPOTTED BY THE RAILROAD ON THE PACKING HOUSE SPUR AS A PROSPECTIVE SPOTTED CAR. ALSO INCLUDED IN THIS AGREEMENT WAS A MINIMUM $100 FREIGHT DAMAGE OR LOSS CLAIM, REGARDLESS OF THE CAUSE OR RESPONSIBILITY; A LIMIT OF FOUR MONTHS TO FILE RAIL CLAIMS, COMPARED TO THE INDUSTRY STANDARD OF TWO YEARS AND A DAY; THE SHIPPER WOULD BE LIABLE FOR CARS THAT WERE NOT UNLOADED BY THE RECEIVER ON TIME; THE CARRIER COULD REQUIRE FULL PAYMENT BEFORE SHIPPING, NO MATTER WHAT YOUR CREDIT RATING OR PAST PAYMENT HISTORY; AND THE CARRIER COULD SEIZE YOUR LOAD FOR UNSETTLED CLAIM DISPUTES.

THE TERMS OF THIS AGREEMENT WERE CLEARLY TO A DISADVANTAGE OF THE GROWER/SHIPPER AND SUNKIST REFUSED TO SIGN. UNFORTUNATELY, WITHOUT A SIGNED AGREEMENT, THE SOUTHERN PACIFIC THREATENED TO CUT OFF THEIR RAIL SERVICE OVER NIGHT. WITH THOUSANDS OF CASES OF PERISHABLE ORANGES SITTING ON LOADING DOCKS OF PACKING HOUSES, THIS CAPTIVE SHIPPER HAD NO TRANSPORTATION ALTERNATIVE.

MR. CHAIRMAN, THESE EXAMPLES ARE JUST THE TIP OF THE ICEBERG. CLEARLY, NO RAILROAD SHOULD BE PERMITTED TO MONOPOLIZE THE RAIL SHIPMENTS OF PERISHABLE COMMODITIES OR ANY INDUSTRIAL GOODS. FURTHERMORE, NO RAILROAD SHOULD BE ABLE TO THREATEN TO SUSPEND SERVICE OF A SOLE RAILROAD FACILITY. OUR INDUSTRY IS NOT SEEKING REGULATION. WE MERELY SEEK COMPETITION. AND IT IS OUR BELIEF THAT S. 447 WOULD RETURN COMPETITION TO THE RAIL INDUSTRY.

FINALLY, MR. CHAIRMAN, LET ME CONCLUDE WITH A SHORT NOTE ON A VERY IMPORTANT SECTION OF S. 447, THE LEGISLATION THAT PERMITS ANY PERSON INJURED BY A VIOLATION OF SUBSECTION (a) TO BRING ACTION FOR INJUNCTIVE RELIEF AS PROVIDED UNDER SECTION 16 OF THE CLAYTON

ACT. AS A PERISHABLE GROWER AND SHIPPER, THIS PROVISION IS ESSENTIAL TO RETURNING COMPETITION TO THE RAIL INDUSTRY. MY AGRICULTURAL COMMODITIES DO NOT PERMIT ME THE LUXURY OF LENGTHY RATE NEGOTIATIONS. IF MY CROPS ARE ROTTING AT THE DOCK, I MUST AGREE TO THE RAILROAD TERMS.

YOUR SUPPORT IS URGENTLY NEEDED TO HELP RESTORE COMPETITION TO OUR NATION'S CAPTIVE RAIL SHIPPERS. THANK YOU FOR YOUR ATTENTION AND I WOULD BE HAPPY TO ANSWER ANY QUESTIONS.

Southern Pacific Transportation Company

1667 K Street, N.W., Suite 600, Washington, D.C. 20006

Wiley N. Jones
Assistant Vice President
Governmental Relations

(202)
393-0100

September 26, 1985

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Chairman Thurmond:

Pursuant to our conversations with Mr. Ken Starling of the Committee Professional Staff, the following statement is submitted for inclusion in the record for the hearings held on S. 447 on September 24, 1985.

As our statement is related to the testimony given the Committee by the United Fresh Fruit and Vegetable Association, we respectfully request that the Southern Pacific Transportation Company statement be included in the record immediately following the United Fresh Fruit and Vegetable Association material.

We appreciate this opportunity to present our views to the Committee.

Sincerely,

Wiley N. Jones

Wiley N. Jones

STATEMENT OF
DENMAN K. MCNEAR
CHAIRMAN, PRESIDENT AND CHIEF EXECUTIVE OFFICER
SOUTHERN PACIFIC TRANSPORTATION COMPANY
BEFORE THE
SENATE COMMITTEE ON THE JUDICIARY
SEPTEMBER 24, 1985

Mr. Chairman and members of this Committee, I appreciate this opportunity to present the views of Southern Pacific Transportation Company on issues relating to S. 447.

We, of course, concur in the statement earlier submitted by Mr. Dempsey on behalf of the Association of American Railroads. Southern Pacific strongly endorses Mr. Dempsey's assessment that S. 447 would result in essentially duplicative maximum rate regulation which - upon close examination of the facts - is wholly unnecessary.

Some of the so-called "facts" which you have before you for review are allusions to two pricing actions of Southern Pacific found in the September 24, 1985 statement of the United Fresh Fruit and Vegetable Association ("UFFVA").

I believe that a close scrutiny of those two situations will bear out the position of the Association of American Railroads and Southern Pacific that legislative action such as S. 447 is unnecessary.

The UFFVA's statement essentially addressed the rail transportation of fresh fruits and vegetables. This market must be placed in perspective at the outset.

Through the first half of this century, railroads handled a large portion of the transportation of fresh fruits and vegetables from the growing areas to the consuming areas of this nation. Consistent with their position in the marketplace as well as the obligations imposed by regulation, the railroads maintained a fleet in excess of 100,000 cars to handle these commodities and attempted to adopt a pricing structure to support the economics of equipment ownership along with a reasonable profit, although with limited success.

Beginning in the 1950's, the rail transportation picture changed dramatically. With the construction and maintenance by the Government of the Federal Interstate Highway system and with Government approval for increased truck size and weight limits, motor carriers were placed in a position to offer competitive services. The motor carriers' position was further enhanced by the disparity in regulatory treatment between the trucking and rail industries. The motor carriers were exempt from economic regulation while the railroads remained fully regulated.

In 1951, U.S. railroads handled 71% of all perishable traffic. By 1977, the rail market share had dropped to 15%.

Southern Pacific Transportation Company serves some of the most productive growing areas in the nation in California and Arizona, and, as such, is one of the principal rail carriers of fresh fruits and vegetables. During that same interval, from 1951 to 1977, Southern Pacific's share of the total U.S. market dropped from 20% to 8%.

At the same time that railroads were losing market share, the intensive price competition from unregulated motor carriers was forcing railroads to set rates at levels which did not economically support the maintenance of a large (and relatively unused) fleet of refrigerator cars. By 1977, the rail refrigerator car fleet had been reduced to less than 31,500 cars.

In 1978, the rail industry's revenue/variable cost ratio for fresh fruit and vegetable transportation was only 119% for fruits and 110% for vegetables. (Potatoes showed a slightly higher revenue/variable cost ratio of 117%). The railroads were essentially only breaking even and were clearly not obtaining revenues sufficient for the purchase of new equipment.

In an attempt to stem the decline in rail transportation, the Interstate Commerce Commission decided the following year to exempt rail fresh fruit and vegetable transportation (excluding potatoes) from regulation. (Rail General Exemption Authority - Fresh Fruits and Vegetables, 361 ICC 211 (1979)). In proposing the exemption, the ICC noted that:

> "The Secretary of Agriculture estimates that
> approximately 90 percent of the fresh fruit and

> vegetable traffic moves by exempt trucks. Similarly, the Rail Public Counsel concludes that in 84.1 percent of more than 2,000 cases analyzed from USDA data, the railroad share of the national transportation market for fresh fruits and vegetables is less than 10 percent." (Ex Parte No. 346 (Sub-No. 1), Rail General Exemption Authority - Fresh Fruits and Vegetables, served December 6, 1978, pg. 2: fn. 1)

In July, 1979, the revenue/variable cost ratio for the rail transportation of potatoes using current costs was only 103.6%. The railroads were again operating at only marginal economic levels. Moreover, rail market share was showing a steady decline. In 1972, rail carriers handled 31% of all potato movements. By 1977, however, the share had dropped to 17.8%. In some states such as California, the railroads accounted for a somewhat larger share, but it was still relatively low and it was also declining. In 1972, the California rail market share for potatoes was 35.4% and by 1977, it had dropped to 29.4%.

The following year, 1980, the ICC granted an exemption for the rail movement of potatoes in Ex Parte No. 346 (Sub-No. 2) Rail General Exemption Authority, Miscellaneous Commodities, served March 24, 1980. In its decision the ICC stated:

> "Statistics submitted by a number of parties indicate that since 1972, rail participation in potato movements nationwide had declined approximately 40 percent, and tonnages originated by rail decreased approximately 54 percent between 1967 and 1977. DOA unload statistics show that the rail percentage of total unloads in 1975 and 1977 was only 19 percent. While these figures are nationwide in scope and do not reflect higher unload figures from some geographic regions, particularly on long-haul movements from the west and midwest to the east (primarily from Idaho and North Dakota) they are indicative of the increasing reliance by shippers on other transportation modes to move potatoes nationwide to the detriment of railroads. Even when considered on a regional basis, the rail market share does not exceed traditional standards indicating market power and lack of effective competition." (Id. pg. 11-12 footnotes omitted)

Notwithstanding the exemption of virtually all fresh fruits and vegetables, the rail market share for the transportation of those commodities has continued to decline. By 1984, the rail market share of fresh produce shipments was only 7.1% and it is forecasted by the U.S. Department of Agriculture to continue to decline to only 6.6% in 1985.*/ At the same time, the nation's refrigerator car fleet has dropped to less than 12,000 cars.

It is in the context of this minimal and declining market share for perishable transportation that the specific factual situations mentioned by the UFFVA should be considered.

The first situation involved the rail transportation of California potatoes. The UFFVA asserted in its statement that:

> "Potato growers are bulk captive shippers since the volume, commodity weight and distance of haul are adoptable only to the economies and efficiencies of rail transportation. Trucks, at most any price, could not even make a respectable dent in our transportation needs."

However, the facts do not bear out this statement. According to U.S. Department of Agriculture statistics,**/ approximately 75% of the potatoes grown in the United States last year were transported from the growing areas by motor carriers. The so-called captive potato growers used the railroads for only 25% of their shipments. For potatoes grown in California, the truck market share is only slightly less. Again, based upon USDA statistics**/ only 31% of California potatoes moved last year by rail with the remaining 69% moving by truck.

The plain truth is that California potato shippers can and do use trucks to meet most of their transportation needs. However, focusing on a very limited segment of the total transportation market, the UFFVA goes on to say that:

> "Southern Pacific carload rates for potatoes shipped from California to consumers in Boston increased from $6,960 on May 27 to $9,860 on June 17. During the same period, rates for Idaho potatoes traveling a similar distance on the Union Pacific Railroad remained a constant $5,750. A difference of $4,110 per carload!"

At the outset, it should be noted that the Union Pacific is essentially the only railroad serving the Idaho potato shippers and yet the UFFVA not only does not object to the UP's rate actions, but even holds that railroad out in favorable comparison to SP's actions. Apparently, the availability of two railroads is not the factor causing Idaho shippers to obtain lower rates.

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*/ Agriculture Outlook, Economic Research Service, United States Department of Agriculture, July, 1985, p. 21.

**/ U.S. Department of Agriculture's Fresh Fruit and Vegetable Arrival Totals For 22 Cities, (Market Service Branch, Washington, D.C., FVAS-3 Calendar Year 1984)

Let us turn, however, just to SP's rate actions. Traditionally, California potatoes are harvested and shipped only during the 2-month period of May and June each year. Unlike growers in Idaho who ship throughout the year, the California potato shippers do not have cold storage facilities which would allow year-round distribution of shipments. As a result, California potatoes do not move during the other ten months of the year and the refrigerator cars and other rail facilities used for potato shipments must remain idle or SP must find alternative uses for the assets.

Partially as a result of the sporadic demand for transportation and use of its equipment, Pacific Fruit Express ("PFE") - which is the subsidiary of Southern Pacific charged with marketing and providing perishable transportation - has lost during the last six years from 1979 through 1984, over $15 million, with the losses escalating in the last year to approximately $9.9 million.

At the same time, Southern Pacific's overall financial position has deteriorated sharply to the point where it is losing money from all operations. SP's income from operations declined to a deficit of $143.2 million by 1983. SP's rate of return on investment was a negative 1.89 percent in 1983. Over the past ten years, Southern Pacific's rate of return on investment has fluctuated at depressed levels and has averaged only 1.72%. SP, therefore, could not subsidize its perishable operations even if it wanted to.

In anticipation of the 1985 season, and with the hope of realizing some profit on potato shipments, Pacific Fruit Express reviewed both the long-term and short-term transportation outlook with California potato shippers. The review was made with individual shippers, as well as a representative organization of some potato shippers, the Western Growers Association ("WGA").

As part of its review, Pacific Fruit Express offered contract rates to WGA as well as to individual shippers. The main thrust behind these alternatives was that if the shippers could give PFE assurances upon which it could base more efficient car supply planning, the cost savings would be passed on to the shipper in the form of lower rates.

PFE offered three alternatives:

- PFE offered to contract with WGA itself if WGA could lawfully contract for its members. PFE received no response from WGA to this offer.
- PFE offered full-year contracts with rate caps. Certain shippers took advantage of these contracts and their rates were $5,800 per carload to Boston compared to the spot market rate for shippers with no contracts of $9,860 during the peak of the season.
- PFE offered option contracts in May to shippers who did not want full-year contracts. These options provided special rate caps in return for guaranteed shipments at specific times. Certain shippers also took advantage of these contracts and those shippers paid $8,990 per carload for shipments to Boston during the peak period in lieu of the spot market rate.

The result was that shippers were offered alternatives to the higher spot market rates. Some shippers took advantage of the alternatives and paid lower rates. Those shippers also received a guaranteed car supply. Those shippers who elected not to sign a contract and those who would not commit to transport guaranteed volumes of traffic via SP paid the higher spot market rate if they wanted to move their shipments by rail rather than by truck.

The spot market rate was not excessive even when compared with the cost of the movements. For example, the rate cited by UFFVA of $9,860 to Boston resulted in a revenue/variable cost ratio for the railroads on such movements of only 162%! This must be compared to the revenue/variable cost ratio of 180% which has been established by Congress in the Staggers Act (49 U.S.C. § 10709) as the statutory minimum threshold test for finding a lack of effective competition on regulated rail traffic. (If the revenue/variable cost ratio for traffic is currently less than 180%, there is essentially a conclusive presumption that effective competition for the traffic exits or that the market position of the carrier has not been employed to obtain revenues out of line with cost and revenue requirements.)

The facts are that Southern Pacific offered rates in line with those of other railroads such as UP if the shippers would work with SP to ship a reasonable level of business throughout the year (as the Idaho shippers provide to Union Pacific) rather than just during the short California growing season. The rail costs associated with a twelve-month versus a two-month shipping season are radically different. Those shippers who have complained about SP's actions, were unwilling to make any commitment and, in effect, are demanding the same rates given to shippers who are able to offer the railroad a twelve-month shipping season.

Regrettably, all that the above explanation shows is that the rail transportation of perishables, including potatoes, faces long-term problems which require long-term solutions. For example, even with the new rate structure, the average revenue/variable cost ratio for all of SP's actual potato movements during the 1985 season was less than 128%.

In an attempt to resolve these problems, SP has asked WGA to work with us to seek a solution. We have offered to sell cars to WGA if, through lower labor costs, they can maintain cars in an economically viable manner. Pacific Fruit Express would then manage the cars. A draft agreement was forwarded to WGA for their review in May, but there has been no response to SP to date. PFE has also offered long-term contracts, if lawful, for WGA's consideration. Again, there has been no response to date.

Southern Pacific has asked WGA to join it in a study to explore the practical and economic use of intermodal equipment for perishables including the new "double stack" cars.

It remains Southern Pacific's hope to ship potatoes at a reasonable profit while keeping California growers competitive in their historical markets. Southern Pacific has opened discourse on the issues with shippers and has offered initial alternatives in the hope of attaining these goals. It is clearly a mutual concern of both the railroad and the shippers, and Southern

Pacific awaits a constructive response from the involved shippers.

Turning to UFFVA's second example: it was asserted that Southern Pacific threatened to:

> "...cut off service to a number of captive shippers if they did not agree to new master transportation agreements, written in their corporate offices without the benefit of meaningful discussions and negotiations with shippers."

That clearly did not happen and the actual facts prove the incorrectness of UFFVA's assertions.

First, Sunkist - who was asserted to be the "captive shipper" in this instance - is the largest transporter of fresh citrus products (primarily oranges, grapefruits and lemons) from the State of California. And according to U.S.D.A. statistics,*/ approximately 59% of those citrus products move from the packing houses in California by truck. For the so-called captive citrus shippers which include Sunkist, only 41% of their product moves by rail in both carload and trailer-on-flat-car service.

Since January 1984, Pacific Fruit Express had approached Sunkist and offered to enter into a contract for their perishable transportation needs. However, no contract was consummated and, instead, Sunkist continued to use PFE's public circular setting forth rates and conditions of transportation for those shippers who were unwilling to commit by contract to ship an agreed upon volume by rail and who desired to use rail only as stand-by service when trucks were inconvenient or unavailable.

In October 1984, PFE decided to change the terms of its public circular to resolve outstanding problems regularly occurring under the terms of the existing circular as a result of abuses by a few shippers. For example, shippers were sometimes using rail refrigerator cars for storing their product prior to shipment and they were also abusing the payment and claims provisions. I must emphasize that it was only a very few shippers who caused these problems, but they exacerbated an already critical situation for SP and PFE.

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*/ U.S. Department of Agriculture's Fresh Fruit and Vegetable Arrival Totals For 22 Cities, (Market Service Branch, Washington, D.C., FVAS-3 Calendar Year 1984)

Pacific Fruit Express notified all shippers who used the public circular in October that 30 days later on November 16, 1984, the terms of shipment would be changed.

Along with this thirty-day notice period, PFE again reminded Sunkist of its long outstanding offer to enter into a negotiated contract. It was plainly stated to Sunkist and all other similarly situated shippers that all of the terms of the public circular were negotiable for those shippers who would commit to use rail on a guaranteed basis instead of on a stand-by basis when trucks were not available.

(I must comment here also that contrary to UFFVA's assertions, no new "master transportation agreement" unilaterally dictated by PFE was offered in November 1984. Only a revised public circular was made available to shippers.)

In response to PFE's notification to Sunkist of the terms of the new public circular and PFE's offer to negotiate a contract, Sunkist advised PFE by letter that it would not accept some of the terms of the new circular and would continue to ship by rail under such terms as it (Sunkist) unilaterally revised.

Regrettably, PFE had no choice but to advise Sunkist that it could not accept Sunkist's demands. Such action would have placed Sunkist in a more favorable position than any other non-contracting shipper.

Since Sunkist plainly notified PFE that it would not abide by all of the terms of the public circular, PFE advised Sunkist that unless it revised its position, PFE could not accept Sunkist's products for shipment. It was not until the day before the new circular was to become effective that Sunkist finally notified PFE it would abide by the terms of the public circular.

While it is certainly regrettable that a misunderstanding may have occurred at the time with one of Southern Pacific's valued customers, we believe it is necessary to treat all of our customers fairly and impartially. If Southern Pacific changes its public circulars, it makes the change for everyone.

At the same time, Southern Pacific stands ready to enter into contracts to meet individual shipper needs when such shippers are willing to commit traffic to SP. I am pleased to say that I believe Southern Pacific's and Sunkist's mutual problems relating to the circular have been resolved. We have recently entered into a contract which covers the outstanding issues between us and will hopefully lead to the increased rail transportation of Sunkist products in the future.

To briefly summarize, I believe that when the facts involving rail transportation are critically reviewed, it can be readily seen that there is no need for remedial legislation such as S. 447.

This statement has been submitted because Southern Pacific was named as the cause of a problem for allegedly captive shippers in two instances. As I have shown, not only were the shippers not captive, but there was no problem that good faith negotiations between the parties could not have been resolved.

Southern Pacific is committed to providing the best service possible for its customers while earning a reasonable compensation for its services. If a shipper has a problem regarding rail transportation, it is also our problem and we aggressively strive to work out negotiated solutions with those shippers. It is my understanding that Southern Pacific has more contracts with shippers than most other railroads.

Based upon the two examples submitted by UFFVA, legislation such as S. 447 is certainly unnecessary. And I believe, when you look at situations involving other railroads, you will reach the same conclusion.

Once again, I join with Mr. Dempsey of the Association of American Railroads and urge you to reject legislation such as S. 447.

Thank you.

Senator DECONCINI. Mr. Johnston, thank you very much and my apologies for thinking you were Mr. Milan Yager, a gentleman I think I know. You are far better looking; I should not have mixed you up.

Mr. JOHNSTON. Somewhat older, also.

Senator DECONCINI. Mr. Loos, do you have any statement that you care to make before we begin the questions?

STATEMENT OF DICKSON LOOS

Mr. LOOS. Well, Senator, I would like to point out that perishables, and the perishable industry which Mr. Johnston represents, have had the longest experience with deregulation.

We were deregulated by Commission order, I think, in 1979. We have therefore, probably, more experience with the difficulties in dealing with a monopolistic situation than probably any other industry, and Mr. Johnston has detailed certain specific instances of abuses of market power which your bill I think is designed and will correct.

Senator DECONCINI. Mr. Johnston, can you give us the status, and I know it is outlined in your statement of perishable commodity growers, when the ICC has exempted railroads from regulation in the handling of perishable commodities. Can you give us one example for the record, here, of what happened, and also, when doing that, what recourse you and your association and members have.

Mr. JOHNSTON. Mr. Chairman, this past spring and summer, as a potato shipper in Kern County, we experienced some considerable losses of sales of our commodity in the Eastern markets because of the rapid escalation in pricing, sometimes equaling over $1,000 a week in escalation of prices.

It had the effect of demoralizing——

Senator DECONCINI. Excuse me. What does that amount to in terms of percentage increase?

Mr. JOHNSTON. We experienced—well, yes, we experienced rates from around $5,000, from Bakersfield, CA, to Boston, and within 3 weeks period of time, that increased to roughly $9,800 over a 3-week period of time.

Senator DECONCINI. You are talking about a 20-percent rise in a week?

Mr. JOHNSTON. Twenty-percent rise in a week. Our customers could not absorb the rapid price escalation. Our commodity being a rather cheaply sold commodity on a per pound basis could not absorb the differences, prices dropped drastically, and ultimately, the growers in our area abandoned and left in the field approximately 5 million hundredweight of potatoes.

Senator DECONCINI. Primarily because they could not afford to ship them to the east coast?

Mr. JOHNSTON. Yes, sir. In my opinion it was all predicated by the fact that we did not have adequate rail transportation at reasonable prices.

Senator DECONCINI. Did you consider any other alternative?

Mr. JOHNSTON. We had no alternative, we had no legal recourse with the railroads, we attempted to set up a dialog with the railroads which was a complete and total exercise in futility.

Senator DECONCINI. Would you say their attitude was, "That's tough?"

Mr. JOHNSTON. Their attitude was that the railroads were in trouble, particularly in perishable transportation, they did not have adequate equipment, and they had no money to rebuild it, and they were going to charge these exhorbitant rates, so they said, to make a profit for the railroad so that they could continue in the perishable business.

Senator DECONCINI. Do you have any reason to believe——

Mr. JOHNSTON. We have a differing view of course about that matter. They have announced, repeatedly, that they do have—they have no intention, whatsoever, of rebuilding equipment to haul perishable goods.

So, our response to them was, why, then, the exhorbitant rates, if you are not going to replace the equipment? They had no answer to that question.

Senator DECONCINI. And what did they answer to that question?

Mr. JOHNSTON. They had no answer to that question at all.

Senator DECONCINI. Do you have any reason to believe that they lost money?

Mr. JOHNSTON. We had a competitive situation that I could cite to you, where the Union Pacific Railroad, and the Burlington Northern, operate out of northwestern United States, primarily Idaho and Washington.

They were shipping into the same markets for roughly 50 percent of what we were shipping for, $5,000 compared to——

Senator DECONCINI. You mean costwise?

Mr. JOHNSTON. Yes. I think the rate out of western Idaho at that particular time was $5,700 per carload, and at the same time we were paying close to $10,000. Obviously, the customer is going to buy——

Senator DECONCINI. But I think both those railroads have been profitable.

Mr. JOHNSTON. They indicate that they have, and they also have some new shiny equipment which indicates to me that they are doing pretty well.

Senator DECONCINI. Mr. Chairman, I see you have arrived. If you want to usurp your——

Senator GRASSLEY [presiding]. Well, I would just as soon have you complete your questioning. I will have two questions I will ask when you are done.

Senator DECONCINI. All right. Thank you. Let me ask one more question. Mr. Johnston, can you give us the specifics of what this would mean to the Southwest growers?

Mr. JOHNSTON. Specifically, in my industry, which is the potato industry, and of course probably to a lesser degree the citrus industry.

But I think that the Western Growers Association is going to be bound by the responsibility to recommend to those growers that they reduce their acreage by at least 50 percent, not to accommodate the marketplace, but to accommodate the transportation system.

Senator DECONCINI. Mr. Bagalay, you indicated the $20 million, extra cost in transportation. Was that over a period of a year?

Mr. BAGALAY. Yes. One year.

Senator DECONCINI. And did you also indicate that you had competition at one time?

Mr. BAGALAY. We had no competition.

Senator DECONCINI. You had no competition on the transportation?

Mr. BAGALAY. We had no competition when we were dependent upon a source of coal in which there was no rail competition.

Senator DECONCINI. And now there is competition?

Mr. BAGALAY. And now we have competition. We have got two vigorously competing railroads both of which we do business with, and we reduced our transportation charges by $5 a ton, overnight.

Senator DECONCINI. Do you have any reason to believe that those railroads are not doing well?

Mr. BAGALAY. If they are not doing well, I do not know why they are so interested in our business, and interested in the business of the major metropolitan areas of Texas.

Senator DECONCINI. Indeed, they are very competitive, obviously, in trying to get you to use them to haul your coal.

Mr. BAGALAY. Absolutely.

Senator DECONCINI. That is what this competitiveness is all about.

Mr. BAGALAY. I agree.

Senator DECONCINI. Mr. Fogarty, have you had any experience talking to other State transportation authorities regarding this legislation, and can you express any of their opinions, or do you have any?

Mr. FOGARTY. Mr. Chairman——

Senator DECONCINI. Did they oppose this legislation, or support it?

Mr. FOGARTY. I visited with a couple of them, and I think at the point that we talked with them, which was maybe 2 months ago, they were not that conversant with the legislation.

Senator DECONCINI. What about the Midwest? Can you comment on the rail rate experience in the Midwest States?

Mr. FOGARTY. I can comment as Montana's rates relate to the Midwest, as you know, the Montana grain producers had filed a class action lawsuit against the Burlington Northern in 1980. As part of this rate case study which has now been going on for about 4 years before the ICC, and has cost the State and the grain growers in excess of $500,000, for this particular point in time, we found that our rates, shipping hard red wheat to the Pacific north coast points, were 240 percent of revenue to variable cost versus the systemwide average for BN of 185 percent.

But other carriers were carrying grain like distance, like weights, for 114 percent. So, our rates are considerably in excess of other States that have competition.

Senator DECONCINI. Yes. So the competition works, with that example.

Mr. FOGARTY. In our judgment, it is the key.

Senator DECONCINI. Mr. Johnston, going back to you, would you give me an opinion—and maybe Mr. Loos can help—on whether the merger of the Santa Fe and Southern Pacific Railroads will adversely impact on the perishable commodity growers in the Southwest?

And also, would this legislation assist them?

Mr. JOHNSTON. First of all, I think, Mr. Chairman, I would comment by saying that virtually the rail merger has been complete, they are operating as if they are one at the present time, so I really feel that there would be no particular difference.

The perishable industry throughout the country I think is opposed to the merger, based upon the grounds that they have no competitive rails in the event that there is a merger.

I am sure Mr. Loos would have a comment.

Mr. LOOS. Well, the merger is viewed as a very, very adverse impact on perishable shippers in the west coast and also in the Southwest, particularly in the west coast, where there used to be two side-by-side railroads competing for the perishable business, where there used to be five or six or seven good overland routes to the East and to the Midwest. We are now going to be confronted with one system, that is, the Santa Fe system, and, we would have virtually no choice in routings. We would have no chance to use, which at one time, was considered one of the most efficient routes, the SP, and then the UP, and the Chicago Northwestern into Chicago. That certainly would be out of the question.

And without some means for the sole facility, that is to say, the Santa Fe line, to be used by the connecting lines, we would have no rail transportation alternative. So I think that——

Senator DECONCINI. Will this legislation assist?

Mr. LOOS. This legislation would certainly assist. I think it is the only thing we see as a viable alternative, because, you see, we are exempt. Whatever may be done in the regulatory field will not help us. We have to rely on your bill.

Senator DECONCINI. Thank you, gentlemen. Thank you, Mr. Chairman.

Senator GRASSLEY. Before I ask questions, I would like to call attention to both panels today, as well as members of the committee, that I held a hearing in Waterloo, IA, on this very subject, on August 29, and I do not know whether the record is available yet, but it may be something that you would wish to refer to as well.

Senator DECONCINI. I would like to see it, Mr. Chairman.

Senator GRASSLEY. Well, then let me see if I can get our staffs together to get that to you.

I would like to know in what ways, is the current antitrust law inadequate to provide protection for rail shippers.

Mr. LOOS. Well, I will take a crack at it first. I think probably the most, so far as the perishable industry is concerned, the inadequacy now is the—and difficulty, if not impossibility of getting injunctive relief.

You see, when you have perishable shipments such as Mr. Johnston was referring to, you have produce coming out of the ground and off the trees, and you have very little time to do anything.

You take what the railroads give you, you need rail cars, and there is no forum for injunction. Under the scheme that has existed for many years, the only agency which had exclusive injunctive power was the Interstate Commerce Commission, and so you have in the law, in the antitrust law—I think it is in section XVI—now a prohibition against injunctions against railroads.

Probably the Arrow Transportation Co. case in the Supreme Court, I think, laid out in specific detail the congressional purpose, which was to have a fast method of injunctive relief for a length of time, specific length of time, so as to maintain the status quo. Well, we would like, and under this bill that Senator DeConcini has introduced, we think we would have the right, when a situation such as was outlined by Mr. Johnston, to go to court and get an injunction to maintain the status quo, while the parties would negotiate a reasonable rate.

That is what we consider to be the main weakness in the present law.

Senator GRASSLEY. Do any of you want to tackle it, or is that answer adequate for all of you?

[No response.]

Senator GRASSLEY. OK. Then my second point would be in regard to the fact that the Interstate Commerce Commission has, underway, proceedings dealing with both market dominance and with competitive access.

Now, we have been informed today that evidently that deliberation is done, that they have not issued an opinion yet, and that they will attempt to get that information to us very quickly.

But from the standpoint of market dominance and competitive access, and the hearings of the Interstate Commerce Commission, is it possible that those proceedings will solve some of the problems being discussed at this hearing?

Mr. FOGARTY. Mr. Chairman, I would like to respond to that, if I could. The State of Montana did participate in the Ex Parte 456 hearings which I believe you are referring to, and it is our judgment that there is no adequate resolution going to come out to the problems.

We think it is going to have to be addressed by the Congress.

Senator GRASSLEY. And that is on both of those points, of market dominance and competitive access?

Mr. FOGARTY. Yes, sir.

Senator GRASSLEY. OK. Does anybody else have anything to add to that?

Mr. LOOS. Of course, so far as the perishable shippers are concerned, we are exempt. Whatever the Interstate Commerce Commission does will not help us.

Senator GRASSLEY. OK. Please proceed.

Mr. BAGALAY. Your two questions, the first and the second ones are, I think, related. They both are economic in nature and have legal implications, and I am not really positive, for example, that I have the economic wisdom to speak to the structure of a capital-intensive industry such as the railroads.

But the essential issue, it seems to me, is one of competitive access. I am not particularly troubled by an industry that may be better economically served, and the preservation of our capital market resources through mergers, or the reduction of the numbers of entities involved in it. But it seems to me that whether it be by the regulatory process, or by the antitrust laws, that the issue of competitive access is the essential issue, and that from my point of view, it makes very little difference how you achieve it.

Perhaps there is a dual approach there. I cannot speak to the question, whether the ICC hearings, on its rulemaking, will accomplish that result, but the bottom line, so far as the shipper is concerned, is to obtain the most effective way of the injection of competition into an industry which has been remarkably, I think, characterized by the absence of it in recent years.

Senator **Grassley**. I am going to ask unanimous consent that the letter I just mentioned, from the Commerce Commission to the chairman, Strom Thurmond, be put in the record at this point. No objection. So that is included.

[The letter follows:]

Interstate Commerce Commission
Washington, D.C. 20423

OFFICE OF THE CHAIRMAN

September 23, 1985

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I would like to take this opportunity to provide you with supplemental information regarding the Interstate Commerce Commission's written statement to the Committee last spring on the Railway Antimonopoly Act, S.447. It is my understanding that this letter will be included in the record of the Committee's hearing on this matter on September 24, 1985.

The Commission's statement to you expressed our general opposition to the bill based on practical problems it could create, as well as its failure to reflect the basic economic policies of the Staggers Act and the balance that was intended in that Act. Our views on this matter remain the same.

As you know, our statement also referred to a pending Commission proceeding, Ex Parte No. 445 (Sub-No. 1), Intramodal Rail Competition, which we felt would be a more appropriate vehicle for the establishment of competitive access standards than the provisions of S.447. The Commission recently voted in an open conference on the various issues raised in that proceeding, and, since a written decision has not yet been published, I would like to briefly summarize the rules the Commission adopted.

These rules include:

(1) The railroads must give 45 days' notice of all cancellations and must provide, within 10 days of request, an explanation and justification for a proposed cancellation of a through route and/or joint rate;

(2) A party intending to initiate a proceeding to challenge a cancellation of a joint rate or seeking the prescription of a through route, through rate or reciprocal switching arrangement, shall first negotiate in good faith to resolve its dispute with the prospective defendants;

(3) The Commission will suspend a proposed cancellation of a through route and/or joint rate where: (1) the cancellation would eliminate effective railroad competition; and (2) the shipper or railroad meets the requisite standing requirements;

(4) The Commission will find the cancellation of a through route and/or a joint rate contrary to the public interest if it violates the competitive policies of section 10101a or is otherwise anticompetitive;

(5) The Commission will prescribe a through route or a joint rate under section 10705, or reciprocal switching under section 11103, if the prescription is necessary to remedy or to prevent an anticompetitive action, and a shipper or carrier meets the requisite standing requirements;

(6) In making determinations concerning investigation or prescription in competitive access cases, the Commission will not consider product competition. In addition, railroads wishing to rely on geographic competition will have the burden of proving the existence of such competition by clear and convincing evidence; and

(7) The Commission adopted the policy that determinations in competitive access proceedings will not be given any *res judicata* or collateral estoppel effect in any litigation involving the same facts or controversy arising under the antitrust laws of the United States.

Another rulemaking proceeding (Ex Parte No. 320, (Sub-No. 3), *Product and Geographic Competition)* recently voted on by the Commission also may help accomplish some of the goals of S.447. Since there is not yet a published decision in that proceeding either, I would also like to summarize the Commission's rulings on various issues involved there.

These rules make it easier for a shipper to show that it is captive by:

(1) putting the burden of proving the existence of effective geographic or product competition on the railroads in all market dominance proceedings;

(2) stating that the fact a railroad faces geographic or product competition with respect to a receiver will not, in and of itself, establish the existence of effective geographic or product competition in relation to a producer, and vice-versa;

(3) placing the burden of proof on the railroads to show that receiver alternatives effectively restrain railroads vis-a-vis producers, and vice versa;

(4) combining the present product competition guidelines' language into a concise summary which more clearly reflects present policy; and

(5) combining, summarizing, and revising the phrasing of the present geographic competition guidelines for greater clarity and better reflection of present policy.

We will, of course, supply the Committee with our formal decisions in these two proceedings when they are available, which I hope will be in late October. Prior to that time, we will be only too willing to provide you with any additional information you may want.

If I can be of any further assistance, please contact me.

Sincerely,

Reese H. Taylor, Jr.
Chairman

Senator GRASSLEY. We will say thank you to you for your participation, and remind you that there may be some questions coming to you in writing, we would ask that you get those answers returned to us in 15 days. Thank you.

We are going to have the next three witnesses come as a panel. Spencer Wendelin, director of strategic planning, the Pittsburgh and Lake Erie Railroad in Pittsburgh; William Dempsey, and he is president of the Association of American Railroads; and James A. Calderwood, and he is with a law firm here in Washington, DC, of Grove, Jaskiewicz, Gilliam & Cobert.

We would ask you to proceed in the way that I introduced you. So, would you proceed, then.

STATEMENT OF A PANEL CONSISTING OF SPENCER N. WENDELIN, DIRECTOR OF STRATEGIC PLANNING, PITTSBURGH & LAKE ERIE RAILROAD, PITTSBURGH, PA; WILLIAM H. DEMPSEY, PRESIDENT, ASSOCIATION OF AMERICAN RAILROADS, WASHINGTON, DC; JAMES A. CALDERWOOD ESQ., GROVE, JASKIEWICZ, GILLIAM & COBERT, WASHINGTON, DC

Mr. WENDELIN. Mr. Chairman, I have a written version of my testimony which I would like to ask be submitted as a part of the record. In any case, good morning, Mr. Chairman, Senator DeConcini.

My name is Spencer Wendelin. I am director of strategic planning for the Pittsburgh & Lake Erie Railroad.

The P&LE is a regional carrier whose 500 miles of track serve customers in western Pennsylvania and eastern Ohio, and via trackage rights, we serve the coal and ore docks at Ashtabula, OH, and beyond, to Buffalo, NY.

I am here today to express P&LE's views on Senate bill 447 which is currently before this committee. Some background on the competitive problems within our industry will be helpful in understanding my comments.

The primary problem of competition with the industry is centered around the market foreclosure activities of the major carriers, which have not only been condoned, but in fact encouraged by the Interstate Commerce Commission. These mega-carriers have instituted, and the ICC has blessed, such major anticompetitive activities as massive joint rate and route closures, and the economic foreclosure of local competitive access through the use of monopolistic pricing practices on reciprocal switching.

Conrail has been a principal architect and perpetrator of these anticompetitive actions, and I will be happy to go into some examples of that, if the committee wishes.

The Interstate Commerce Commission in approving these reductions in competition has used inconsistent and confused logic to circumvent the pro competitive intent of Congress as expressed in the Staggers Rail Act of 1980.

The results of the ICC's actions in this area can only be termed as incredible. The ICC, as Senator Grassley noted, has just concluded 2 years of hearings on the competitive access issue, by adopting rules as vague and meaningless as those which it was using prior to the hearings.

Gentlemen, I wish to assure you today, that these regulations will not be effective in solving the competitive access problem, nor will they promote competition within the industry.

The P&LE participated in those hearings as a member of the RAM group, or Railroads Against Monopoly. That group includes the majority of all regional railroads within the country.

These carriers are also members of the American Association of Railroads, or AAR. However, we do not support the AAR's policy stance on this vital competitive access issue.

In fact when my distinguished colleague, on my left, Mr. Dempsey, speaks to you about the competitive access issue, he is forced to express the views of the largest carriers in the industry which control 85 percent of all railroad business, and therefore, the voting structure within the AAR.

It is no coincidence that the regional railroads, whose shippers are most vitally impacted by these anticompetitive activities on the part of the largest carriers, are the railroads promoting true competition.

The regional railroads are least able to play the market allocation games being played by these largest railroads.

In fact, the shipping public is being de facto allocated among these largest carriers with little input in the process. This is creating more captive shippers.

Our economy, gentlemen, is suffering from enough competitive disadvantages today. We can neither afford, nor allow the construction of artificial barriers to competition within the vital transportation sector, upon which every other part of the economy depends for essential services.

Let there be no mistakes today, gentlemen: The regional carriers, such as the P&LE, are faced with economic strangulation. Effective action to cure these problems is needed and it must come soon.

However, we do not believe that Senate bill 447 forms the primary solution needed for this problem. The P&LE's objections to this legislation fall primarily into three areas.

First, it would tend to insert the courts as a referee into highly technical railroad operating and compensation issues not normally within the courts 'expertise.

Second, we are concerned about the potential criminal liability, implications contained in the legislation.

And last, as a businessman, let me assure you that the solution to this problem should not be centered on protracted litigation.

We need a solution to the problem which will allow us to respond to the marketplace on an everyday basis, and often, on a yesterday timeframe.

We believe that the most effective fix for these problems lies in first, modernizing the remainder of the Interstate Commerce Commission Act, by extending the procompetitive Staggers Act policies to the entire ICC legislation.

Second, to have the clearest and most irrevocable expression of congressional intent sent to the Interstate Commerce Commission—promote railroad competition—and lastly, to have this Senate review each nominee for the Interstate Commerce Commission that comes before it, to ensure that those nominees are fully sensitized to this vital competitive access issue, prior to receiving your approval.

Thank you, Mr. Chairman, Senator DeConcini, for your vital interest in this question, and the opportunity to come and express our views on it today.

I would be happy to answer any questions that you may have, and as I indicated before, I have a written statement which I would ask to be included in the record as part of my testimony.

[The statement follows:]

STATEMENT OF

SPENCER N. WENDELIN, DIRECTOR OF STRATEGIC PLANNING PITTSBURGH AND LAKE ERIE RAILROAD COMPANY

Mr. Chairman and members of the Committee, my name is Spencer N. Wendelin. I am Director of Strategic Planning for the Pittsburgh & Lake Erie Railroad Company ("P&LE") and I wish to express my gratitude and appreciation for being invited to testify at the behest of the Committee in connection with Senate Bill 447.

By way of background, P&LE is a common carrier regional railroad operating approximately 500 miles of track and providing service over 240 miles of main line in the western Pennsylvania, eastern Ohio region of the United States. Its lines extend from Connellsville and Brownsville in southwestern Pennsylvania through Pittsburgh and Aliquippa, to Youngstown, Ohio. From there, P&LE provides freight service north via long term trackage rights over Conrail to iron ore and coal docks at Ashtabula, Ohio and northeast from Youngstown via similar trackage rights over Conrail through Sharon, Pennsylvania to a connection with the Bessemer and Lake Erie Railroad at Shenango, Pennsylvania. P&LE also operates on trackage rights over the Norfolk and Western Railroad Company for shipments of coal via Ashtabula to Buffalo, New York. P&LE is presently one of two regional railroads which has negotiated a divestiture agreement with the Norfolk Southern Corporation to acquire additional lines of railroad in our regional markets as part of the Conrail sale transaction which is currently under consideration by the Congress.

Today, my testimony will address the serious anti-competitive problems which have arisen in the railroad industry as a result of the action of certain Class I mega-railroads. Through the cancellation of joint rates and routes and the termination or monopolistic pricing of reciprocal switching, these giant railroads have severely curtailed competitive access of regional railroads to off-line markets. In reviewing these actions, the Interstate Commerce Commission has ignored the competitive dictates of Congress set forth in the Staggers Rail Act of 1980. The Commission has permitted competitive foreclosure of joint rates and routes without any precancellation investigation into the facts of particular situations or the competitive impact on shippers and carriers affected by these actions. The basic principal of transportation deregulation is to "let the market be the regulator". When this principle is applied to the railroad industry, it presupposes open market access to all competitors. Allowing unsupported and unsupportable foreclosure of competition through blanket rate and route cancellations clearly flies in the face of this tenant and makes a farce of "regulation by market forces".

P&LE and other regional carriers have been the primary victims of the Commission's policy of permitting indiscriminate, blanket cancellation of joint rates and routes without careful examination of individual routing efficiencies. P&LE is actively litigating interterritorial cancellations of joint rates and routes in ICC Docket 38676, Changes in Routing Provisions -- Conrail -- July, 1981, and intraterritorial joint rate and route cancellations in ICC Docket 39176 (Sub-No. 1), Pittsburgh and Lake Erie Railroad Company v. Consolidated Rail Corporation. In these proceedings, P&LE, other regional carriers and shippers have challenged the legality of the Commission's current policy of reducing railroad competition by permitting indiscriminate blanket cancellations which result in the elimination of efficient, as well as inefficient, joint rates and routes. Before the ICC in Ex Parte 456, The Staggers Rail Act - Conference of Interested Parties, and Ex Parte 455 (Sub-No. 1) Intramodal Rail Competition, P&LE and other regional carriers have contended that without specific procedures to adequately measure comparative routing efficiencies and a fair opportunity to investigate the competitive impact of rate or route cancellations before they become effective, there is no way by which shippers and regional carriers can retain efficient, competitive routing alternatives in the face of the massive market power wielded by the six Class I mega-railroads which together control in excess of 85% of all railroad business in this country.[1]

Let there be no mistake, regional railroads are today faced with the threat of economic strangulation as a result of the ICC's failure to take effective action to curb blanket cancellations of joint rates and routes. The large mega-railroads have marshalled various economic theories and experts to justify their actions, but there is a wide desparity between those espoused economic theories and their day-to-day business practices in the competitive marketplace. A brief look at P&LE's experience indicates why we are vitally concerned with the competitive access problem.

P&LE traffic consists primarily of bulk volumes of coal, coke, scrap, iron ore and semi-finished iron and steel products. A small portion, perhaps 15%, of our business involves a wide variety of industrial products for shippers both large and small. Such traffic is nevertheless important to P&LE in terms of the revenue it provides. However, from 1980 to the present, P&LE has seen a precipitous decline in its car loadings and total revenues. The following figures depict this reduction.

Fiscal Year	Car Loadings	Gross Revenues (in thousands)
1980	271,436	77,864
1981	256,190	80,189
1982	167,283	52,759
1983	126,042	38,323
1984	149,164	52,663

Carloadings for 1985 indicate further traffic erosion. Approximately 30% of P&LE traffic historically involved local business which originated and terminated on P&LE lines; and 70% involved interline business with other railroads, mainly

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[1] These railroads include Consolidated Rail Corporation, Norfolk Southern Corporation, CSX Corporation, Burlington Northern Railroad Company, Union Pacific/Missouri Pacific Railroads and Santa Fe Southern Pacific Corp. (merger application currently pending before the ICC).

Conrail, N&W, and the Chessie System. As local steel markets in the Pittsburgh area have contracted, P&LE and its customers have become even more dependent on its connections.

The volumes of traffic interchanged with Conrail have been especially important to P&LE. To a large extent, P&LE traffic interchanged with Conrail reflects the historic market relationships that P&LE had built through years of affiliation with Conrail's predecessor railroads. Thus, Conrail, an amalgamation of six northeast railroads, operates an extensive rail network that serves most of the shipping points within the Northeast which provide important markets for P&LE customers. In many cases, Conrail is the only railroad which serves these northeastern markets.

In 1979, the number of cars interchanged between P&LE and Conrail at Youngstown, Ohio rank seventh among all rail interchange points in the entire nation. That same year, P&LE and Conrail interchanged an additional 21,000 carloads of freight at other junctions. An indication of the importance of Conrail to P&LE is demonstrated by the following interchange statistics for the years 1979 through 1984. The figures listed below indicate the car loadings and revenues received by P&LE for shipments which it originated or terminated jointly with Conrail during those years.

Year	Interchange Carloads	Gross Freight Revenue (in thousands)
1979	101,223	24,918
1980	49,627	13,647
1981	43,845	13,833
1982	13,184	4,712
1983	13,797	5,747
1984	17,177	7,207

These carload and revenue statistics indicate the magnitude of the market for joint line rail service between P&LE and Conrail. They also demonstrate the drastic decline in traffic handled with Conrail on a joint line basis particularly after the effective dates of Conrail's route cancellations.

Although P&LE and Conrail can work together on joint line traffic, Conrail also operates its own competing lines which parallel virtually every foot of P&LE main line. In fact, P&LE and Conrail serve fourteen common, competitive points. Several of the major industrial shippers served by P&LE operate industrial switching railroads which also interchange directly with Conrail. Conrail's blanket cancellation of joint rates and routes with P&LE has enabled it to continue to serve these points with its own single-line routes while eliminating competitive P&LE-Conrail joint routes. The cancellations have been sanctioned by the ICC regardless of the comparative efficiencies of these alternative routes and contrary to the express congressional intent to encourage interrailroad competition. As can be seen by the foregoing statistics, it is absolutely essential and vital to P&LE's continued existence that it have efficient, competitive joint rates and routes with all of its connecting carriers by which its customers can reach origin and destination markets beyond present P&LE rail lines.

As noted above, the Interstate Commerce Commission has failed to promote competition within the railroad industry. In fact, recent ICC decisions have had the opposite effect of reducing interrailroad competition. Over the last two years P&LE has participated with a group of other regional railroads ("RAM -- i.e. Railroads Against Monopoly") in a prolonged series of administrative hearings before the Interstate Commerce Commission. These hearings created a voluminous record of the anticompetitive abuses of the Class I mega-railroads. RAM proposed administrative procedures and regulations which would have remedied these problems. However, the Commission has now rejected these proposals. Instead, it adopted a vague set of guidelines which will prove impossible to enforce consistently and will make it more difficult for regional carriers and shippers to combat anticompetitive foreclosures on the part of large railroads. The record in those ICC proceedings indicates clearly that regional carriers foresaw this result and recognized that the mega-railroads would use these ICC proceedings to delay legislative efforts necessary to address these problems. Two years later these predictions have become reality.

Moreover, any hope which may have existed on the part of regional railroads and rail dependent shippers for increased

Commission sensitivity to competitive access issues has been dashed by recent ICC decisions in Pittsburgh and Lake Erie Railroad Company v. Consolidated Rail Corporation, Docket 39176 (Sub-No. 1) April 9, 1985; appeal pending Pittsburgh and Lake Erie Railroad Company v. ICC, No. 85-1312, (C.A.D.C.) and Midtec Paper Corp., et al v. Chicago and Northwestern Transportation Company (Use of Terminal Facilities and Reciprocal Switching Agreement) Docket 39021, July 17, 1985; appeal pending, Midtec Paper Corporation, et al v. U. S., No. 85-1476 (C.A.D.C.). In those two decisions the majority of the Commissioners have indicated that they are completely reconciled to the anticompetitive conduct of the mega-railroads and are interested only in guaranteeing the revenue adequacy of these largest railroads.

Given the severity of our problems and the current predisposition of a majority of the Interstate Commerce Commission, P&LE welcomes the attention and consideration being given to competitive access problems by the Senate Judiciary Committee. P&LE has encountered first hand the same frustration and consternation experienced by many rail dependent shippers with current ICC policy. We understand the desire to seek alternative solutions to competitive access problems through the application of the antitrust laws. However in our view, the legislation currently being considered by this Committee will not provide a satisfactory solution to our problems. P&LE believes that the primary approach to correction of competitive access problems is to amend those provisions of the Interstate Commerce Act which the ICC has used to conduct an end run around the procompetitive congressional intent articulated in the Staggers Rail Act of 1980. Let me hasten to add and emphasize that P&LE does not advocate the amendment of the Staggers Rail Act. The legislative changes which we envision would modernize those provisions of the Interstate Commerce Act which predate the Staggers Act and which the Interstate Commerce Commission has used to avoid promotion of vigorous interrailroad competition.

P&LE has reservations about the provisions of Senate Bill 447. Under this bill, any person could obtain trackage rights for a competing carrier despite the fact that the competing carrier may not find the use of the owning railroad's line to be profitable, or consistent with its own operating plan. This provision would require the courts to establish technical and complex operational arrangements between competing railroads and monitor appropriate price levels or compensation arrangements between competing carriers. We question whether the courts are an appropriate vehicle in which to resolve these kinds of controversies. Moreover, the provision, as currently drafted, creates potential criminal liability whenever it is determined that a carrier has denied use of its sole facility "with the effect of monopolizing". The possibility of criminal sanctions for business conduct without regard to the intent of the actors conflicts with fundamental concepts of criminal law.

P&LE also recognizes that antitrust remedies proposed in S.447 would be more expensive, time consuming, and difficult to obtain than working through an effective administrative process potentially available under the Interstate Commerce Act. It is well known that antitrust actions often involve litigation by attrition and in such litigation the regional carriers and small or medium size shippers which are most vulnerable to these market foreclosures are the parties which do not have sufficient resources to prevail against large, well financed railroad defendants.

In conclusion, P&LE wants this Committee to know that the competitive access problems which we and our customers face are serious. They result, largely, from the Interstate Commerce Commission's failure to effectively implement a procompetitive rail transportation policy as intended by Congress in the Staggers Rail Act of 1980. The most direct way to solve that problem is for Congress to enact limited but specific legislation which will ensure that the procompetitive rail policy and intent of the Staggers Act is uniformly and rigorously administered by the ICC under all sections of the Interstate

Commerce Act. Also, when consideration is given by the Senate to confirming appointments to the Interstate Commerce Commission, it should insure that the candidates nominated for those positions thoroughly understand the need for a fair and equitable administration of competitive rail transportation policy. As long as these remedies are possible, P&LE can not support the legislative proposal presently before this Committee in S.447.

Mr. Chairman, members of the Committee, once again I wish to thank you for this opportunity to present testimony on this very important issue and express my appreciation for your interest in these matters. If you have any questions, I will be more than happy to attempt to answer them for you at this time. Thank you very much.

Senator GRASSLEY. Mr. Dempsey.

STATEMENT OF WILLIAM H. DEMPSEY

Mr. DEMPSEY. Thank you, Mr. Chairman. I am glad to be here again to express our views at the association on what is a modified form of the antimonopoly bill.

We opposed the bill in its prior version and we oppose it in its present version, and I will just indicate, very swiftly, why that is.

I should note that I have already put in a great deal of evidence with respect to railroad rates, and I will simply rely upon the evidence that I have already introduced.

I think the only development of any significance, since I testified last, primarily on coal rates, has been that the Department of Energy has conducted a very lengthy and detailed study of that issue, and in particular, looked at those examples that were cited to it as being examples of abuse by railroads of monopoly power, and they concluded that, indeed, our position was correct, and I will just read two sentences out of their draft report.

"The study found no evidence that railroads have imposed abusive rates on coal since 1980"—which of course was the date of the Staggers Act—"and even in cases where rates have risen, the increases do not appear to have been widespread or of great magnitude."

As to grain rates, I would want to look at the testimony that was introduced this morning and perhaps I may ask for permission to put in a response to that. I would say, though, in general, that we have gotten very few complaints about grain rate and grain transportation since Staggers, and the reason is perfectly clear.

Grain rates, on average, have gone down 18 percent, not in real terms, in actual terms. As to the fresh fruit and vegetable matter, again, the Southern Pacific has a statement which they introduced into the House record, and I expect they will want to introduce the same statement here.

I might note, though, that the rate that is being complained of there is a low rate, even after it was escalated. It came out at about 162 percent, revenue to variable cost ratio, which is well under the jurisdictional threshold established under the Staggers Act. So it is conclusively presumed to be a reasonable rate.

There is a feature of that particular market that the committee should know about. As opposed to the Northeast market, in this area there is only a 2-month shipment period for transportation of fresh fruits and vegetables. Accordingly, as the rates respond to markets, they go up during that 2-month period of time.

The Southern Pacific offered contract rates which were substantially the same as the preexisting rates for guaranteed shipments. Some shippers took those contracts; others, not willing to make that commitment did not. It is a little bit curious to me as to why this particular market is involved in this hearing, since the predicate for exemption of fresh fruits and vegetables is that that is a highly competitive market, and indeed, the railroads carry only something in the way of 25 percent of potatoes out of that market, and in general, our market share is down to about 14 percent. Trucks carry the vast, vast bulk of that traffic.

And now the bill, as revised. It seems to me that there are three fatal flaws in it that have not been corrected by the revisions.

In the first place, there remains an inevitable tension, and indeed, inevitable conflict between this bill, and the Interstate Commerce Act, as amended.

The consequence would be that railroads would be acting at their peril, treble damage peril, criminal action peril. They could very well be charging rates that the Interstate Commerce Commission, under Staggers, would hold to be reasonable, but that would be held to be unreasonable under this bill.

I think if one looks at the explanation accompanying the bill, the inevitable collision becomes quite clear. The explanation, in part, says that there would not be a violation of the act, if the railroads are charging rates that—and I quote—"reflect the effective competition." Now I am not clear, exactly what that means, but the thrust of it is pretty evident, I think, and that is that there would be a determination of illegality, if the rates were higher than one would expect to see in a competitive environment.

Now that is precisely a standard that the Commission will not, and has never applied to railroad rate regulation. The Commission has consistently held that differential pricing, under which rate levels will depend upon market conditions, and the presence or absence, or relative presence or absence of competition, is a necessary principle for the railroad industry to apply, and it is of course applied by all industries in nonregulated environments.

Second, in examining and determining whether or not rates charged by railroads under this bill would be legal, or not, the courts would be undertaking a task that they have consistently abstained from taking in the past, and for very good reason.

That is to say they have not found it within their jurisdiction, under the Sherman Act, to determine whether or not a rate of a monopolist is too high, or not too high. I have cited the relevant authorities and quoted from them, at some length, and I will simply refer you to that. Let me simply read from my testimony a representative statement, though, from one authority.

The question is:

> Does a monopolist which obtains power lawfully violate Section 2, if it exploits its power by pricing at any of the supercompetitive levels which it might rationally choose? . . . [T]he considerations which weigh against it are forceful, indeed, overwhelming. . . . Courts would be asked to act like public utility commissions, policing the business decisions of every patent monopolist, every firm dominating a thin market, and every holder of a scarce resource, to see that prices did not yield more than a reasonable turn on investment.

And finally, that departure from well-established antitrust law would be applicable only to the railroad industry.

Now I suggest that if there is good reason to cast aside this well-established principle for the railroads, then there is good reason for every other industry in the United States, and that at a minimum, the bill should be redrafted, and reconsidered, so that it is of general applicability, and I have in mind particularly the utility industry, which operates in far more monopolist markets than the railroads. I think that concludes what I would have to say, Mr. Chairman. Thank you.

[The following letter was subsequently supplied for the record:]

ASSOCIATION
OF AMERICAN
RAILROADS

William H. Dempsey
President

October 16, 1985

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Chairman Thurmond:

I refer to your letter of October 1, forwarding five questions from Senator DeConcini to which you have asked me to respond. Senator DeConcini's questions and my responses are enclosed.

During the hearing on September 24, William J. Fogarty of the Montana Department of Commerce presented testimony purporting to show that the Burlington Northern's rates in Montana were unduly high because of the absence of competition. I am enclosing a comment I have received from the Burlington Northern which addresses that contention.

The United Fresh Fruit and Vegetable Association also testified at the hearing on the 24th about the rates for shipping potatoes from California to eastern markets, the potato growers allegedly being "captive shippers" of the Southern Pacific Railroad. The President of the Southern Pacific, Denman K. McNear, has filed with the Committee a statement commenting on that Association's testimony. Because Senator DeConcini expressed concern with the potato situation -- and I was not familiar enough with the facts to respond fully -- I would like to highlight a few of the points made by Mr. McNear:

1. The so-called captive potato growers in California shipped 69 percent of their crop by truck in 1984.

2. California potatoes move only during a two-month period because, unlike Idaho growers, the California growers do not have cold storage facilities. Thus, the special rail equipment necessary to handle the California crop is idle ten months of the year unless alternative uses for it are found.

3. Shippers were offered contracts which provided reduced rates in exchange for volume guarantees. Those rejecting a contract were deliberately accepting the risk of higher prices in the spot market.

4. Even at the spot market price, the revenue-to-variable cost ratio of the rate was well below the jurisdictional threshold for rate regulation and, therefore, conclusively presumed to be constrained by competition.

5. The subsidiary of the Southern Pacific responsible for marketing and providing transportation for perishable commodities lost $9.9 million last year.

In short, like so many other critics of the Staggers Act, what the California potato growers seek is not competition but the good old days of regulation when railroad services were required to be available on a stand-by basis at going-out-of-business rates.

Sincerely,

encls.

Questions Asked by Senator DeConcini
and
Mr. Dempsey's Responses

Question 1:

Most industries such as automobile manufacturing, steel producing, the airlines, chemicals and others are subject to the antitrust laws. What makes railroads so special that they should remain largely exempt from the antitrust laws?

Response:

The antitrust laws are fully applicable to the railroad industry except as to those activities where an express exemption from the antitrust laws has been provided by statute or where the regulation of those activities by an administrative agency under another statutory regime has been deemed to displace the antitrust laws in favor of exclusive regulation by that agency.

With respect to the matters of reasonable rates and trackage rights that are the subject of S. 447, the Interstate Commerce Act provides for comprehensive regulation of rates and trackage rights where Congress has deemed it necessary and appropriate. This detailed regulatory scheme was designed to provide and does in fact provide ample protection against alleged abuses of monopoly power and reflects the realization -- less often true today than it was years ago -- that, in some circumstances, railroads may have "natural monopolies." It also reflects the realization that the nation needs a strong and integrated rail system. None of the other industries mentioned in the question are subject to such a regulatory regime. That is what makes the railroads "special" in those areas where they are exempt from the antitrust laws or from certain antitrust remedies.

While supporters of S. 447 have expressed dissatisfaction with the way in which the Interstate Commerce Commission is performing its regulatory role -- wrongly in our view -- no critics have proposed doing away with the Interstate Commerce Act and thus treating the railroads, with all their special characteristics, as the industries mentioned in this question are treated.

Question 2:

I understand certain railroads are subsidiaries of companies or are corporately related to other companies which produce particular commodities transported by the railroad such as coal or lumber. Is there any provision of law preventing such a railroad from contracting with its corporate affiliate to haul particular commodities at lower rates than other producers of the same commodity are charged or to, in effect, charge the non-affiliated shipper so high a price that his product could not compete with that produced by the railroad affiliate?

Response:

Current law does constrain a railroad from attempting to use its market power for the benefit of an affiliate. First, Section 10713 of Title 49, which provides for rail transportation contracts, assures non-affiliated shippers the opportunity to receive the same rates and services for transportation of agricultural commodities, including lumber, as offered to a competing railroad affiliate. For example, if a railroad were to offer its affiliate a reduced rate under a transportation contract for lumber, a competing shipper could challenge the contract as unreasonably discriminatory. If the contract is unreasonably discriminatory, the Commission can require the railroad to offer comparable rates and service. Alternatively, a competing producer may seek to have the contract disapproved by the Commission by demonstrating the contract constitutes a destructive competitive practice.

Second, the antitrust laws prohibit a railroad from using its market power to grant reduced rates to an affiliate to drive the affiliate's competitors out of the marketplace. When a railroad did attempt to discriminate in favor of its coal producing affiliate the Supreme Court found that the railroad had violated Section 2 of the Sherman Act. (See United States v. Reading Co., 253 U.S. 26 (1920)). Given the massive treble damages which would result from this type of violation, the antitrust laws today provide a practical and effective bar to any railroad even attempting to drive its affiliates' competitors out of business

In addition to the legal provisions in place today to protect the interests of shippers competing with railroad affiliates, commercial realities prevent a railroad from discriminating in favor of its affiliates. Given the competition between mines located on different railroads, it would be economically irrational for a railroad to decline to offer competitive rates to any mine on its lines which a coal purchaser identified as a source for its coal needs. No railroad could rely on the coal purchaser selecting its affiliate over coal producers on the lines of competing railroads and, therefore, a railroad must do all it can to promote all coal producers on its lines.

Question 3:

I understand that some railroads have begun to restrict the use over their lines of rail cars not owned by that particular railroad or another major railroad. There are many shippers and short line railroads that own or lease their own railcars. At least in the past shippers often received lower rates for providing their own equipment. Don't restrictions like this enable railroads to further exploit shippers and hinder the operations of short lines?

Response:

I am not aware of any recent activities by railroads to restrict the use over their lines of cars owned by others. The use and pricing of cars is, however, a matter integrally related to the marketing of rail services and there could be developments of which I am not aware. In any event, because the ICC has jurisdiction over the use and pricing of cars, I do not believe the railroads are in a position to exploit either shippers who own cars or short line railroads who lease cars.

While railroads are required to interchange cars with other railroads, they have always had the right to determine whether and the conditions under which private cars would be allowed on their tracks. The Interstate Commerce Commission and the federal courts have long recognized the common carrier obligation of the railroads to provide cars and the concomitant right of the railroads to use their own cars in preference to private cars. See, e.g., Atchison, Topeka & Santa Fe Ry Co. v. United States, 232 U.S. 199, 214-15 (1914); Use of Privately Owned Refrigerator Cars, 201 ICC 323, 373-74 (1934).

Litigation is currently pending before the Commission in which a group of private owners of covered hopper cars has argued that extenuating circumstances warrant a change in the right of the railroads to supply cars. (ICC Docket No. 39169, Shippers Committee, OT-5 v. the Ann Arbor Railroad et al.) The covered hopper car owners argue that the railroads have not met their common carrier obligation to supply covered hopper cars and so have lost their right to supply those cars. In fact, the railroads have purchased an enormous quantity of covered hopper cars based on their needs and the needs of their customers.

Because shippers, leasing companies, and other private investors have also purchased many covered hopper cars, there exists a sizable surplus of those cars. In the litigation before the Commission, the private covered hopper car owners are seeking a rule guaranteeing use of their cars by the railroads despite the fact that those cars were purchased with no guarantees as to their use by any railroad.

As your question indicates, when private cars are used by a railroad, the car owner is given either a reduced rate or an allowance. An agreement was recently reached between the railroads and tank car owners on a method for computing allowances for tank cars. That agreement is now before the ICC for approval.

Similar negotiations have been conducted with the owners of covered hopper cars but, to date, there is no agreement. Individual railroads remain free, subject to the ultimate authority of the ICC, to pursue whatever policy makes commercial sense to them.

Question 4:

Since passage of the Staggers Rail Act in 1980, in how many cases has the ICC finally found market dominance by a railroad and found the rate being charged was unreasonable?

Response:

The entire Commission has found market dominance by a railroad in eleven cases. In three of those, the rate was found to be *unreasonable*. The rate was ruled *reasonable* on six occasions (two of which have been affirmed by the Court of Appeals, D.C. Circuit). In one case (No. 37516) the complaint was dismissed at the request of complainant before a decision was made as to rate reasonableness. In the other case (No. 38025S) the market dominance finding was appealed to the courts before the entire Commission considered the rate reasonableness issue. The eleven cases were:

Docket No.	Commodity	Rate	Status
No. 36114 (1)	coal	reasonable	aff'd by D.C. Circuit
No. 37276 (1)	coal	unreasonable	pending on remand
No. 37409	coal	unreasonable	pending on remand
No. 37516	iron ore		dismissed per complainant
No. 38025S	coal		on appeal to court
No. 38566	iron ore	unreasonable	on appeal to court
No. 38793	coal	reasonable	pending on remand
No. 38809	coal	reasonable	pending on remand
No. 38946	coal	reasonable	aff'd by D.C. Circuit
No. 39060	coal	reasonable	pending on remand
No. 39071	coal	reasonable	final - no appeal

Out of 79 decisions made by the Commission, a Division of the Commission, one of its employee review boards or administrative law judges, 59 decisions found the railroad to be market dominant. Twelve of 49 decisions on the issue of rate reasonableness (excluding recyclables cases) held the rates in question to be unreasonable.

Question 5:

In the course of your testimony, you indicated that the "essential facilities" doctrine didn't apply to many American industries. Please indicate which industries, other than rail and motor carriage, to which it doesn't apply together with cites to applicable case law or statutory reference.

Response:

I do not recall stating that the essential facilities doctrine did not apply to many American industries. However, it would be unusual to find the elements of an "essential facility" in many industries, as a reading of the cases generally cited for that doctrine will show. See, e.g., *MCI Communications Corp. v. AT&T*, 708 F.2d 108;, 1132-33 (7th Cir.), *cert. denied*, 464 U.S.

891 (1983); Otter Tail Power Co. v. United States, 410 U.S. 366 (1973).

Since a classic example of a "bottleneck" is a single railroad through a narrow mountain pass, where there are no transportation alternatives, see Note, Unclogging the Bottleneck: A New Essential Facility Doctrine, 83 Columbia Law Review 441, 443 (1983), regulation of potential abuses of that kind of monopoly power has always been a central purpose of the Interstate Commerce Act. As I explained in some detail in my September 24th statement, the Interstate Commerce Act already requires of railroads everything that the essential facilities doctrine might require of others, as well as providing for the kind of rate regulation that antitrust courts are ill-equipped to perform.

Comment of the Burlington Northern Railroad on Testimony of William J. Fogarty

Burlington Northern faces competition in all of the states where we originate grain. In Nebraska, we face truck competition, and must compete with other railroads both for traffic to terminals such as Kansas City, MO-KS, as well as export traffic to Gulf Ports and West Coast Ports. From Montana, we are faced with competition from the Union Pacific in the Butte area and from the Soo Line Railroad in the northeast corner. More importantly, however, we face competition across the State of Montana from trucks hauling grain in backhaul service to the Coast and to transfer points on the Columbia and Snake River systems for movement by barge to Columbia River export houses. In fact, during the six-month period of June to December 1980, trucks handled nearly 51% of the wheat shipped out of Montana. During this period the Staggers Act became law, and we established reduced single car and unit train rates on wheat from Montana. Since that time, we have been able to increase the rail share of Montana's wheat shipments by means of more efficient operations and consequently lowered costs, enabling BN to better meet its competition.

As can be seen from the following rate comparison, the cost-based increases were authorized but the marketplace would not allow increased rates if we were going to hold this traffic to rail. It should also be pointed out that the following comparison draws the rates from points in Eastern Montana closer to those applying from the Great Falls-Havre-Cut Bank (so-called Triangle) area. From the nine origins shown as examples, four currently have rates lower than December 1, 1980. Four have rates only slightly higher than December 1, 1980, and one has exactly the same 52-car rates as when the unit train program was established, December 1, 1980.

Origin	52-Car Rates as of 12/1/80	If All Increases Had Been Added	Present	Difference in Rates vs. Great Falls		
				12/1/80	If All Increases Applied	Today
Billings	140¢	176¢	129¢	29¢	36¢	13¢
Bozeman	115	145	120	4	4	4
Glendive	170	214	169	59	76	53
Great Falls	111	141	116	-	-	-
Havre	126	159	126	15	19	10
Kalispell	99	124	98	Lower	Lower	Lower
Miles City	165	208	154	54	68	38
Plentywood	168	211	169	57	71	53
Wolf Point	159	201	161	48	61	45

RESULT OF RATE ACTIVITY

Our activities have increased our market share of both total wheat moved out of Montana and specifically wheat destined to coast points only because we offer the best transportation package--not because we're the only carrier. Unit train shipments have made it possible for greater wheat shipment from Montana than could otherwise have been made. Total shipments and rail handling have grown quite large without the chronic car shortages that existed in the late 1970's.

We know that unit train shipments, specifically 52-car shipments, now have a major share of the marketplace due to cost effective rates and services. We also now realize that 52-car shipments are the basis for trading wheat on West Coast exports. For example, on October 12, 1984, the cash price offered at Great Falls for 11% protein, hard red winter wheat was $3.47 per bushel. At Portland, the first half October delivered price was $4.22 per bushel (it has been $4.24). The difference between $4.22 at Portland and $3.47 at Great Falls is 75¢ per bushel or $1.25 per cwt. The Great Falls 52-car rate is $1.16 per cwt., leaving 9¢ for handling, elevation, etc. Thus making it clear that the most efficient form of transportation, i.e., 52-car shipments, set the price for Montana's wheat.

Most important, however, is the improvement in price received by the producer, which we can estimate. Historically, before unit trains, the single car basis would factor into the origin vs. destination pricing of grain. Today's single car rate from Great Falls is 153¢ per cwt. This converts to 22¢ per bushel. If we are now handling over 95 million bushels of Montana wheat westbound by rail, and if the 52-car basis is used for grain pricing, then $20 million dollars are now passed on to producers in the form of higher grain prices due to our unit train program. That's $20 million dollars every year that are left in the State of Montana for other purposes.

Senator GRASSLEY. Mr. Dempsey, thank you very much, and we will have questions after we hear from Mr. Calderwood.

STATEMENT OF JAMES A. CALDERWOOD

Mr. CALDERWOOD. Thank you, Mr. Chairman.

My name is James Calderwood. I am an attorney. I specialize in the application of the antitrust laws to transportation industries.

I spent 8 years as a trial attorney with the Department of Justice in the Antitrust Division, spending most of that time in the transportation section.

Since entering private practice 6 years ago, my field has been almost entirely with the application of the antitrust laws to transportation.

I think one of the basic problems that we are faced with in the railroad market today really comes about from some misconceptions.

When Congress first passed the 4-R Act in 1976, and the Staggers Act in 1980, there was much testimony at that time about the exemption from the antitrust laws for railroads being repealed, and by that they meant the Reed-Bulwinkle Act which allowed railroads to get together and in fact fix prices under ICC jurisdiction, but it was basically legalized price-fixing.

The ability of the railroads to be able to do that, was greatly cut back when the Staggers Act was passed. There was a lot of testimony from Department of Justice officials, and others, at that time, that the antitrust laws would then play a vigorous role. But in fact, the antitrust laws are not permitted to play a vigorous role as they apply to railroads.

It is because there was much more antitrust exemptions for railroads than just the Reed-Bulwinkle Act. The basic antitrust statute, the Sherman Act, which was passed back in 1890, prohibits, in section I, price-fixing, market boycotts, and other agreements in restraint of trade and, section II prohibits monopolization and attempts to monopolize.

But in the *Keogh* decision by the Supreme Court in 1922, the Supreme Court said that because the rates were subject to regulation, or regulated by the Interstate Commerce Commission, that gave an immunity from the antitrust. That was really a judicially created immunity from private antitrust damage suits, and that decision holds firm today.

We have had, just in the last 12 months, three courts of appeals decisions, and one district court decision, all dismissing cases against carriers based on the *Keogh* decision.

So the *Keogh* decision remains very firm law today, and while the Sherman Act, both sections I and II are applicable to most of American industry—everyone from General Motors to Joe's Hamburger Stand, it is not applicable to the railroads, by and large, because of the *Keogh* decision. Only the Department of Justice can bring an action under the Sherman Act against a railroad, and it has brought exactly one case since the Staggers Act was passed in 1980, and my research, to date, I have been unable to find any other Sherman Act case brought by the Department of Justice since the end of World War I.

Section VII of the Clayton Act, the antimerger statute, is another major antitrust statute. This statute provides that carriers regulated by the ICC, that is, railroads, are exempt from its coverage.

The Robinson-Patman Act, the legislation passed in 1938, which prohibits price discrimination in the sale of goods to similiarly situated purchasers, applies only to the sale of goods and has no effect on discriminations in price among railroads or other service industries.

And lastly, the other major antitrust statute is section V of the Federal Trade Commission Act, which outlaws unfair and deceptive practices in commerce. By its very statutory language ICC-regulated carriers, that is, railroads, are exempted from it.

So what we are faced with is a situation today, that even though many Members of Congress felt the railroads would no longer have their antitrust exemption when it passed the Staggers Act in 1980, the basic fact is that the railroads are not subject to them except for possible action by the Department of Justice, and Justice has been extremely reluctant to bring any of those cases.

I would also add as far as injunctions go, section VXI of the Clayton Act prohibits private parties from being able to obtain injunctions under the antitrust laws against railroads, again leaving only the Justice Department with the possibility of an injunction.

Therefore, the railroads maintain a very privileged position in America today. I think as the testimony here in the Senate hearings and the House hearings have very amply demonstrated, the Interstate Commerce Commission simply is not regulating the railroads anymore.

The market dominance standard which would give the ICC the ability to regulate rates, that was put in by Congress to protect captive shippers in 1980, has simply not been used by the ICC.

They have been extremely reluctant to do anything about it. I think the Railroad Antimonopoly Act, the bill now before the Senate, is a very narrow piece of legislation. It is hardly radical in any sense.

It is designed to enable shippers who are faced with monopoly rail transportation systems, to be able to have some effective antitrust remedy. It basically incorporates the "essential facilities" doctrine, something announced by the Supreme Court back in 1912 in a case against railroads, *United States* v. *Terminal Railroad.*

It is a well-recognized antitrust doctrine, it has been used in any number of cases, in a large segment of industries.

One of the opening remarks referred to, "Why don't we make the essential facilities doctrine?"—I think that is what Mr. Dempsey had in mind—applicable to all of American industry?

It is applicable to the electric utility industry, the industry that he mentioned, because there have been several cases involving that industry.

The *Otter Tail Power* case, one of the leading ones, decided by the Supreme Court in 1973 concerned that industry. There, a community could purchase power at a much cheaper rate from a company other than the monopoly power company it was faced with, and, in that case, the Supreme Court said that the wheeling of power, or transferring of power over the facilities of a monopolist, from an area of cheaper power, would be possible.

So the essential facilities doctrine, a well-recognized part of the antitrust laws, is applicable to the rest of American industry, and this bill would have the effect of applying it to railroads.

For the last part of my opening comment, I would like to give an example. A recent ICC decision involved a company called Midtech Mills, up in Kimberly, WI, a paper processor. What happened was Midtech was served by a monopoly rail carrier, the Chicago & Northwestern.

The Soo Line, another railroad, came along and said to Midtech Mills, "We'll offer you a lower rate. We'll haul your paper at a lower rate than the Chicago Northwestern's charging you."

And Midtech said, "Fine. We'd love that." So they went to the Chicago Northwestern and said, "Well, we have to switch cars. We'd like to use your switching facilities so that we can serve that Midtech plant."

The Chicago Northwestern said, "No, we won't allow you to do it; we want to continue to be a monopoly and we want to continue to earn monopoly profits."

So Midtech and the Soo Line went to the Interstate Commerce Commission and said, "Mr. Commerce Commission, please order the Chicago Northwestern to grant those switching rights."

Traditionally this is the kind of thing the ICC handled, over the decades since the ICC was created in 1887. This is the kind of thing ICC would order. So that monopoly problems would be taken care of.

What did the ICC do in Midtech Mills? In the decision issued this July they said, "No, we won't order it because there's paper produced elsewhere in the United States. We're going to recognize that geographic competition and we won't order any switching. So Mr. Midtech Mills in Kimberly, WI, you can continue to pay the monopoly rates to the Chicago & Northwestern, even though the Soo Line will serve you more cheaply."

I submit that the legislation that we have here, in the Railroad Antimonopoly Act, will take care of those kinds of situations.

It is the kind of situation that the essential facilities doctrine recognizes elsewhere in American industry, and there is no particular reason, I can see, why the railroads should be exempt from this.

And I have a prepared statement which I have submitted, and would be glad to have any questions. Thank you.

[The statement follows:]

LAW OFFICES
GROVE, JASKIEWICZ, GILLIAM AND COBERT
SUITE 501
1730 M STREET, NORTHWEST
WASHINGTON, D. C. 20036

TELEPHONE (202) 296-2900
TELECOPIER (202) 296-1370
TELEX 904058WSH
CABLE AMERICALAW

MANUFACTURERS BANK BUILDING
SUITE 1008
16255 VENTURA BOULEVARD
ENCINO, CALIFORNIA 91436
(213) 872-2202

APPLICATION OF THE ANTITRUST LAWS TO THE RAILROAD INDUSTRY

Prepared testimony of James A. Calderwood, Esquire,* before the Committee on the Judiciary, United States Senate, hearings on S. 447, the "Railroad Antimonopoly Act of 1985," September 24, 1985.

INTRODUCTION

Historically the antitrust laws have rarely been of major importance in the legal atmosphere in which railroads operate. The nation's first national regulatory agency, the Interstate Commerce Commission (ICC) was established in 1887 to control the rail industry. 1/ This was three years before the first antitrust statute, the Sherman Act, was enacted. Hence, from their very beginning, the antitrust laws were not looked upon as the key method of controlling economic abuse by railroads. As Congress recognized various types of railroad problems and as shippers or communities felt a need to have the railroad industry restrained in certain ways additional legislation was passed giving the ICC increasing authority over almost all aspects of rail carrier operations. This included the Hepburn Act in 1906 2/ the Mann-Elkins Act in 1910 3/, and the Transportation Act of 1920. 4/

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* Mr. Calderwood was for many years a senior trial attorney with the Antitrust Division of the Department of Justice. For most of this time he was with what is now the Transportation Section of the Antitrust Division. He is presently the partner in charge of the Antitrust Group of the Washington, D.C. law firm of Grove, Jaskiewicz, Gilliam and Cobert. He has litigated several antitrust cases involving transportation companies and rendered advice to carriers and shippers concerning the antitrust laws and transportation. He has written many articles dealing with antitrust/transportation problems and chairs the Editorial Board of the monthly publication Transportation Antitrust Report. He is an honors graduate of the law school at George Washington University, which he attended on scholarship, and has studied the problems of competition regulation at Oxford University.

Interestingly, some of the earliest Supreme Court cases under the Sherman Act involved rail practices (e.g. United States v. Trans-Missouri Freight Assn., 166 U.S. 290 (1897) and United States v. Terminal Railroad Assn., 224 U.S. 383 (1912)). While these cases found that the Sherman Act applied to railroads (to prohibit price fixing in the first case and to prohibit an agreement among railroads to control access to bridges crossing the Mississippi river in the latter case) it was decided by Congress, early in this century, not to rely upon the antitrust laws to prevent railroad abuse, but instead to enact legislation giving the ICC the authority to regulate most railroad activity.

It developed that if a shipper, equipment supplier, connecting railroad, particular community or anyone else with a real or imagined problem with a railroad wanted to seek legal means to deal with the problem it would approach the ICC and ask that agency to control the situation. The ICC's power over the railroads was pervasive and often utilized. Consequently, there was not, until recently, a significantly felt need to rely upon the antitrust laws to deal with rail carrier abuse.

ANTITRUST OVERVIEW

It is important in analyzing the current state of the antitrust laws as they apply to the railroad industry to understand just what types of practices the antitrust laws apply to with respect to most of American industry and then to see if these antitrust laws apply to these same practices by railroads.

In a nutshell the most important provisions of the antitrust laws are: The Sherman Act which makes unlawful two types of practices: 1. agreements in restraint of trade (e.g. price fixing, group boycotts) 5/ and 2. abuses of a market position (monopolization or attempts to monopolize) 6/; Section 7 of the Clayton Act, prohibiting mergers which may substantially lessen competition or tend to create a monopoly 7/; The Robinson-Patman Act (which is an amendment to the Clayton Act) prohibiting price discrimination 8/ and Section 5 of the Federal Trade Commission Act prohibiting unfair or deceptive acts or practices. 9/ Not only can the Government bring actions against most commercial entities to enforce these provisions, but, with respect to the vast majority of American industry, private parties may also institute damage suits 10/ and injunction actions 11/ (except for the Federal Trade Commission Act under which private suits, either for damages or for injunctions, are not permitted).

THE SHERMAN ACT

As noted, the Supreme Court held in the early days of the Sherman Act that that Act prohibited price fixing by railroads (United States v. Trans-Missouri Freight Assn., supra), and abuses of monopoly power by railroads (United States v. Terminal Assn., supra). However, because of the existence of the ICC and its comprehensive power over railroads, few such cases were brought. It was simply faster and more efficient for shippers and others to proceed at the ICC than to initiate Sherman Act litigation.

Finally, for all practical purposes, private suits against railroads for price fixing or monopolization stopped in 1922 when the Supreme Court held in Keogh v. Chicago & Northwestern Railway, 260 U.S. 156, that railroads were immune from damage awards under the Sherman Act reasoning that to award antitrust damages would frustrate the rate regulation jurisdiction of the ICC. The Court stated in Keogh that if rates, even collusively set ones, were approved by the ICC then no damage action was permitted.

The Keogh decision stands today as a barrier to private Sherman Act litigation against railroads. Recent court decisions have reaffirmed Keogh so that it continues as a major obstacle to instituting antitrust cases against railroads. See Minsky v. Auto Driveaway, 757 F.2d 718 (7th Cir. 1984), cert. denied 105 S. Ct. 435 (Nov. 7, 1984); In the Matter of Wheat Rail Freight Rate Antitrust Litigation, 759 F.2d 1305 (7th Cir., 1985), cert. petition pending No. 85-21; Square D Co. v. Niagara Frontier Tariff Bureau, Inc. 760 F.2d 1347 (2nd Cir. 1985), cert. petition pending No. 85-112; In Re Lower Lake Erie Iron Ore Antitrust Litigation, MDL 587 (E.D. Pa., June 7, 1985). With the Supreme Court's declination just ten months ago to review the *Minsky* decision there are real doubts that the Supreme Court will now change the doctrine on its own.

Hence, unlike most of the American commercial world, the railroad industry does not have to be concerned with private suits for price fixing, monopolization or attempts to monopolize. In addition, by statute, injunction actions by private parties against railroads under *any* of the antitrust laws are not permitted because Section 16 of the Clayton Act 12/ expressly prohibits such actions against ICC regulated carriers accept by the Department of Justice.

When Congress enacted the 4-R Act 13/ and the Staggers Act 14/ it severely restricted the activity of railroad rate bureaus and greatly narrowed the legislative antitrust immunity enjoyed by such bureaus for price fixing. 15/ There is a popular misconception that Congress thereby made the railroad industry subject to the panoply of the antitrust laws. This was definitely not the situation.

While the 4-R Act and the Staggers Act removed much of the statutory antitrust exemption permitted railroad rate bureaus so they could engage in price fixing, it did not by any means restore full antitrust liability to the rail industry. Because of the *Keogh* decision and its recent progeny and Section 16 of the Clayton Act the rail industry remains basically immune from antitrust attack from anyone but the Department of Justice.

One may then ask how active has the Department of Justice been in instituting antitrust cases against railroads since the Staggers Act was passed in 1980? The answer is not very active at all. Since enactment of the Staggers Act, the Department of Justice has brought exactly one antitrust case against rail carriers. 16/ In that case, four of the five defendant railroads plead no contest, which was accepted by the court, and the fifth defendant won at trial with a directed verdict of not guilty.

OTHER ANTITRUST STATUTES

In the beginning of my remarks I mentioned the other most important sections of the antitrust laws in addition to the Sherman

Act. Like the Sherman Act, they are also inapplicable to the railroad industry. Section 7 of the Clayton Act, the statute which prohibits anticompetitive mergers, exempts from its coverage by its very language mergers subject to ICC jurisdiction and railroad mergers are presently subject to ICC jurisdiction. 17/ The anti-price discrimination statute, the Robinson-Patman Act, applies only to the sale of commodities and therefore is inapplicable to transportation services. The Federal Trade Commission (FTC) has no jurisdiction over railroads because Section 5(a)(2) of the Federal Trade Commission Act 18/ exempts ICC regulated entities from FTC jurisdiction.

Consequently, the railroad industry in America today is free from practically all of the provisions of the antitrust laws which apply to most other phases of American business.

MARKET DOMINANCE

I will not here review all the issues involved with market dominance findings by the ICC under the Staggers Act. However, let me briefly outline the problem. Prior to the 4-R Act and the Staggers Act all rail rates were tightly regulated by the ICC. Now under 49 U.S.C. § 10709 the ICC may not find a rate unreasonable unless it first makes a finding of market dominance in accordance with standards stated in that section. Since passage of the Staggers Act in 1980 the ICC has rarely found a market dominance situation and, even when it has, the ICC has always found the rate being charged by the railroad in question to be reasonable. In effect, despite the clear intent of Congress to protect shippers under the market dominance standard from railroad rate exploitation in rail monopoly situations the ICC has failed to take any real action. If anything, the ICC's reaction to the Congressionally imposed market dominance standard has been one of tortured starting and stopping in various proceedings developing evidentiary guidelines which leave it almost impossible for shippers, faced with rail monopolies, to be protected from the imposition of monopoly rates. 19/

THE RAILROAD ANTIMONOPOLY ACT

The railroad industry is in the most advantageous position possible for major American corporations. Because of legislative enactments and judicial interpretations they are free from most of the antitrust laws and the regulatory agency with possible authority over them has so interpreted its own authority as to render it impotent to maintain any control. This legal atmosphere is coupled with an ever more concentrated railroad industry. Railroad consolidations continue with the pending mergers of the Santa Fe and the Southern Pacific, the possible acquisition of Conrail by the Norfolk Southern. This would leave probably six major rail systems operating in the United States.

The simple economic fact is that these railroad consolidations have left many communities with no competitive rail service. Some states are, for all practical purposes, served by only one rail system.

Shippers and communities faced with this railroad market situation have been stymied in their efforts to prevent rail monopoly abuses. They are effectively banned by the Keogh decision from actions under Section 2 of the Sherman Act (the anti-monopolization section), prohibited from bringing injunction actions by Section 16 of the Clayton Act, frustrated at the ICC because of that agency's failure to take any action in the last 5 years to effectively deal with market dominance, coupled with the fact that the Department of Justice has instituted only one antitrust case against a railroad since passage of the Staggers Act and that case did not charge a Section 2 violation.

The Railroad Antimonopoly Act is hardly a radical proposal. Actually, it is a rather narrow piece of legislation which would only make railroads subject to the Sherman Act in a limited manner. If enacted, the railroad industry would continue its privileged position in American industry of being largely immune from the antitrust laws and from effective regulation.

Basically, the bill would legislatively overturn the Keogh decision with respect to Section 2 of the Sherman Act and would also allow injunctive relief to private antitrust litigants when rail monopoly abuse is found. In effect, the bill does this through Congressional recognition of the "essential facilities" doctrine with respect to railroads.

The "essential facilities" doctrine (also sometimes referred to as the "bottleneck monopoly" doctrine) is a long recognized antitrust doctrine which goes back to the 1912 Terminal Railroad Assn. decision, referenced earlier. In that case, the Supreme Court held that it violated the Sherman Act for a group of railroads to jointly control the facilities for rail transportation across the Mississippi river and effectively bar others from using the "essential" facility.

Probably the most succinct case finding a Sherman Act violation due to the denial of access to an essential facility is Otter Tail Power Co. v. United States, 410 U.S. 366 (1973). There the Supreme Court held it was unlawful for an electric utility system operating the only electric transmission system in the region to refuse to transmit power over its lines; such power being cheaper than the price asked by the defendant utility system. Of course, it was recognized that the utility system was entitled to some compensation for the use of its facilities, but the defendant system could not abuse its monopoly position by denying access to its essential facility for transmitting electric power to others.20/

The Railroad Antimonopoly Act would remove the Keogh impediment to bringing essential facility type cases under the Sherman Act when it is established that a particular railroad is the sole rail facility available to a shipper and the railroad is effectively seeking to monopolize or has monopolized rail transportation to a particular destination. If the railroad has established reasonable terms for the use of its monopoly facility it would not violate the Sherman Act. Private litigants would have available both antitrust damage and injunction remedies.

This bill would do no more than make rail carriers subject to essential facility antitrust actions the same as the rest of American industry. It does not create some new theory of antitrust relief and does not make railroads subject to the full range of the antitrust statutes.

CONCLUSION

If the railroad industry wants to function in a deregulated, market oriented fashion then, like other major industries, railroads should be subject to at least a portion of the antitrust laws and shippers given an opportunity to curb railroad monopoly abuses, something shippers cannot now expect the Government to do.

James A. Calderwood

FOOTNOTES

1. Interstate Commerce Act, 24 Stat. 37 (1887).

2. Hepburn Act, 34 Stat. 584 (1906).

3. Mann-Elkins Act, 36 Stat. 539 (1910).

4. Transportation Act of 1920, 41 Stat. 456 (1920).

5. 15 U.S.C. § 1.

6. 15 U.S.C. § 2.

7. 15 U.S.C. § 18,

8. 15 U.S.C. § 13(a)-(f).

9. 15 U.S.C. § 45.

10. 15 U.S.C. § 15.

11. 15 U.S.C. § 26.

12. *id*.

13. Railroad Revitalization and Regulatory Reform Act, 90 Stat. 91 (1976).

14. Staggers Rail Act of 1980, 94 Stat. 1895 (1980).

15. Legislatively sanctioned in 1948 with passage of the Reed-Bulwinkle Act, 62 Stat. 472 (1948), now codified as revised at 49 U.S.C. 10706(a). The Reed-Bulwinkle Act was enacted in response to the Supreme Court's decision in *Georgia* v. *Pennsylvania Railroad Co.*, 324. U.S. 439 (1944).

16. *United States* v. *Baltimore and Ohio Railroad*, Criminal No. 81-396 (D.D.C. filed Oct. 13, 1981).

17. 49 U.S.C. 11343.

18. 15 U.S.C. 45(a)(2).

19. *See* generally *Western Coal Traffic League* v. *United States and the ICC*, 674 F.2d 378 (1982), *modified* 719 F.2d 772 (5th Cir.

1983), *cert. denied*, 104 S. Ct. 2160 (1984) and 719 F.2d 772 (5th Cr., 1983), *cert. denied*, 104 S. Ct. 2160 (1984).

20. For other cases concerning the essential facilities doctrine *see* *Associated Press* v. *United States*, 326, U.S. 1 (1945), *Silver* v. *New York Stock Exchange*, 373 U.S. 341 (1963), and *City of Chanute* v. *Kansas Gas and Electric Co.*, 754 F.2d 310 (10th Cir. 1985).

Senator **Grassley**. I would recognize the Senator from Kentucky.

Senator **McConnell**. Thank you, Mr. Chairman. I have got to run. I just wanted to request permission to put a statement in the record at this point and thank you for that opportunity.

Senator **Grassley**. Thank you very much.

[The statement follows:]

Prepared Statement of Senator Mitch McConnell

Mr. Chairman, I appreciate the opportunity to revisit the issue of anticompetitive forces affecting the railroad industry, especially the capitive shippers for whom the problem is in many instances acute. Though I'm not yet convinced that this bill, S. 447, is the most appropriate vehicle for addressing the problems facing these shippers, I nevertheless commend you and Senator DeConcini for pursuing the problem and the search for an equitable and efficient solution.

As I pointed out at the hearing held earlier this year, the antitrust field is constantly evolving, and though to some extent less rapidly in the field of regulated industries, this is nevertheless true in the railroad industry. Because railroads are an essential facility, it is of course appropriate to require that the rates charged by them are reasonable. Traditionally, the Staggers Act has permitted the application of differential pricing, allowing railroads to act competitively where faced with competition but to charge higher prices where they are not. The result, at least in theory, is a competitive industry within the framework of a regulated one.

While the trend toward consolidation in the railroad industry is one that we view with some ambivalence, it is nevertheless one that is with us to stay. This bill may be an attempt to deny that reality, and if so then I will be unable to support it. Still, the jury is still out, and I look forward to the testimony of the witnesses.

Thank you, Mr. Chairman.

Senator **Grassley**. I have two questions.

Are there some kinds of conduct by railroads, that are not immune from treble damage liability under current law?

And if so, do railroads ever sue each other under antitrust law to recover treble damages?

Mr. **Dempsey**. Well, let me start, if I might, on that question. We have responded at great length in our prior answers to the panel's questions on this very subject, so I will not elaborate on it.

The state of *Keogh* is, as Mr. Calderwood puts it right now. On the other hand, the Justice Department and the Interstate Commerce Commission have petitioned the Supreme Court to review the matter and to reverse *Keogh* in its entirety.

So that all that one can say at the present time is that the future, as to *Keogh,* is uncertain. Second, *Keogh* applies only to rate cases; it does not therefore apply to a case in which a boycott is charged, in which it is charged that there is predatory action to drive out a competitor. The *Pinney Dock* case is a recent example.

Barges have brought cases like that under the antitrust laws. And so it is a barrier at the present time. What will happen to it when the Supreme Court looks at it, no one knows. The argument of course is that—one of the arguments, is that the predicate, the major predicate for *Keogh* has been eroded by the Staggers Act in respect of exempt traffic like fresh fruits and vegetables.

I do not know, incidentally, why they could not get an injunction, since the exception of injunctive relief in section 16 applies only to common carriers who are subject to the provisions of the Interstate Commerce Act.

It is argued that the *Keogh* doctrine is not applicable to contract cases because there, the parties have in effect taken that kind of a case out of the jurisdiction of the ICC.

It is argued that it is not applicable to all cases in which the rates are below 180 percent revenue to variable cost ratio, because none of those rates are subject to regulation by the ICC.

All of those arguments are advanced, and which ones will or will not prevail, no one can tell at the present time.

Beyond that, let me say that I assume that the essential facilities doctrine is applicable to the railroad industry since the *Terminal Railroad* case was the grandfather case.

This bill, I submit, does not simply apply the essential facilities doctrine to the rail industry; if it did, there would be no reason for the bill.

What it does is to go far beyond any of the cases that I have read under essential facilities and make the violation turn upon a judgment by a court as to whether the rate is a competitive rate. *Otter Tail* never did that. The rate was not at issue in *Otter Tail.*

The issue was one of denying to a would-be competitor access to the power necessary to permit competitors. Now was the rate ever in issue in MCI? The question——

Senator DECONCINI. Will the chairman allow me to just follow that thought for just a minute.

Senator GRASSLEY. Senator DeConcini.

Senator DECONCINI. Is your great concern that the courts cannot make that judgment? Why is the railroad industry so fearful of our justice system? Do you think that the courts can not make a decision that would be fair for your clients, as well as the consumers, as well as those who feel that there may be a noncompetitive monopoly that is outside the existing law? Can you explain that?

Mr. DEMPSEY. Yes, I can. I am grateful for your asking the question. It is certainly a fair question. It is essentially the same reason that all of the courts, that I have cited and quoted in my statement, have refrained from getting into that area.

It is a very, very complicated matter to make a judgment as to whether a rate is reasonable or not, and whether a rate at a particular level is one that would, or would not, prevail in a competitive market.

Senator DECONCINI. So the courts are not up to it?

Mr. DEMPSEY. That is what they have said. They said, basically, we are not up to it. Now, if we are forced into it, if we are forced into it, then of course we will do it, but until the Congress directs us to do it, we need to stay out of it. That is a matter that is more appropriate for regulatory commissions.

One more example of the difficulty and the collision of congressional policies that you would see, is this: In the Staggers Act, the Congress expressly directed the Commission to take into account, in making its rate determinations, the revenue adequacy, or inadequacy of the rail system, and whether the courts would do that, or not, I would not have any idea, but one would not presume that they would.

Senator GRASSLEY. Would you like to proceed.

Mr. WENDELIN. Yes. Senator Grassley, I would just mention, first of all, I am not a lawyer, but I am familiar enough with the issue to answer your question in part: There have been at least two recent cases where railroads have sued each other under antitrust.

There is a present suit pending between the Grand Trunk Western and Conrail. I might mention, the Grand Trunk Western is one of the members of the RAM group. There was also a case about 3 or 4 years ago between a company called Trans-Kentucky Transportation, Inc., and the CSX Co.

In the first case, the *Grand Trunk Western* case revolves primarily around the question of these rate and route cancellations that I mentioned. In other words, market foreclosure on the part of Conrail.

In the case of the second one, TTI versus CSX, a good part of that case involved a number of factors which relate to the issue before you today, rates and routes, but there were also some issues revolving around what might be called essential facilities in that case.

I might just add something in commentary to what Mr. Dempsey said about the charge of the Commission to ensure revenue adequacy. Let me just say that I think one of the problems with what has happened in the industry is that the Commission has gone overboard in that area, to the extent of ignoring a charge to also promote competition within the industry, to the extent that what we have now in the Commission is a situation where we are not creating any incentives to run our companies with greater efficiency. We are merely putting ourselves in a position where we can say, if a certain joint rate or route is inefficient, we ought to be able to cancel it. The Commission has thereby destroyed the balance between competition and revenue adequacy charges to it from Congress.

There is now no incentive to make a route, or attempt to make more efficient a rate or route before that cancellation takes place. Beyond these comments as I said, I am not a lawyer and am not able to comment on the issue.

Senator GRASSLEY. Mr. Calderwood.

Mr. CALDERWOOD. Yes. I would like to, Senator Grassley, address your question in several different ways. First of all, Mr. Dempsey—I am not sure just what he is referring to in the *Pinney Dock* case, but generally, that means a series of antitrust cases brought against railroads, where they were attempting to keep competitors or private dock operators from hauling iron ore on the Great Lakes.

That case, the private Sherman Act case was dismissed on the *Keogh* doctrine, exactly, by the U.S. District Court for the Eastern District Of Pennsylvania in June of this year.

So, the *Keogh* case has been used to stop the *Pinney Dock* litigation. The only *Pinney Dock* litigation that went forward was the Justice Department's case against those railroads.

That is the one Sherman Act case, since 1918, that this Justice Department has brought, and in that case, the one railroad that went to trial was found not guilty.

The ICC jurisdiction, he mentions, or the argument is put forth, that there are certain categories of traffic to which the ICC—or to which the antitrust laws would now apply. Every time someone considers such a case or brings such a case, the railroads immediately say, "Well, primary jurisdiction over that is with the ICC."

In other words, if you are going to say with respect to anything 180 percent below cost, they will argue that Congress has made and placed in the statute, a finding, that anything below that would automatically not raise any competition problems, and anything above that is with the Interstate Commerce Commission.

One of the reasons we have not seen essential facilities cases since the 1912 *Terminal Railroad* case, is because in 1920, Congress passed the Transportation Act of 1920, which gave the ICC the authority to order switching, and competitive access, exactly the issue in the *Terminal Railroad* case.

And the ICC used to exercise that authority at a time in the past. Also, in talking about the *Grand Trunk* v. *Conrail* case, I think that is an excellent example.

The *Grand Trunk* filed the antitrust case because it was frustrated in trying to get any kind of relief before the Interstate Commerce Commission. And what argument does Conrail use in that case? They are using the *Keogh* decision.

They are using the fact of primary jurisdiction arguments that the case should not be able to proceed. The *Trans-Kentucky* case was settled out of court. I would like to say that this S. 447 is not going to raise the kind of serious antitrust, or overwhelming antitrust issues that have been presented here. I think the language of the act, and of course all statutes, maybe needs some refining before Congress finally votes upon it; but if a railroad has a competitive situation—that is—if we are talking about a category of traffic that can move by another mode, such as the piggyback movements, which are very competitive with trucking—and we have seen a significant reduction in the rates that most railroads charge for trailer and flatcar piggyback service. That sort of thing, if the railroad can establish that it is mode competitive, they would not have to worry about the antitrust cases under this legislation.

The same thing if there is barge traffic available, or a competitive railroad is offering similar service between the same two points in question.

If there is intercoastal steamships available. If there is competition, by mode, traffic available between the same two points, then this statute has a built-in defense to it by the railroads.

It is only going to be in situations where the product in question has no viable alternative, except moving it by a monopoly railroad situation, and if the railroad is earning monopoly profits. Just because you are a monopoly is not going to mean you are guilty. It is only going to mean if you are earning monopoly profits, that you are going to be subject to this statute, and I think therefore, the statute is really narrowly confined to deal with a specific situation.

Senator **Grassley**. Thank you. I have one last question and Senator DeConcini will then adjourn the meeting after his questioning.

I want to thank you for my part, and Senator Thurmond's part, for your participation.

My last question is whether or not it is possible that the ICC's current consideration and proceedings on market dominance and competitive access will solve some of the problems that we are discussing here today.

Mr. **Wendelin**. I will be happy to go first on that, Mr. Chairman. I think as part of my initial statement, you may have heard me indicate that we do not believe that the regulations that were adopted by the Commission last week, and have yet to be made fully public in terms of a written Commission decision, will do anything to mitigate the issue.

They are considerably more vague than are needed and the Commission has let it be known through this proceeding that they are not particularly interested in being tied to anything more specific than the regulations they were using before. So, from our standpoint, we do not believe that these new ICC rules will deal with the issue at all.

Senator DECONCINI [presiding]. Mr. Dempsey.

Mr. DEMPSEY. Those are very complicated questions and I am glad to have a chance to speak to them because I was involved as a principal in the negotiations that led to the proposed rules in both the market dominance proceeding, and the competitive access proceeding, and I must say, as a personal matter, I am distressed, of course, that the rail industry is not united on these issues, but on the other hand, that does happen, even in our industry.

Let me begin with the market dominance question. I do not really think there is a serious market dominance problem, so it is a little hard for me to address the question.

The railroads have lost most of the market dominance cases before the Commission. I do not mean that the Commission has determined the rates to be unreasonable, but they have taken jurisdiction in a considerable majority of the cases in which market dominance was an issue.

So, I have never felt that there has been a basis for complaint by the shipping community. On the other hand, we recognize that there were complaints, and so, with the National Industrial Transportation League, which is far and away the largest umbrella shipper group, the paper industry, and the chemical industry, we worked out proposed rule changes on market dominance. The big issue here has always been whether or how to consider the existence and effect of geographic and product competition.

We agreed to take the burden of proof on those two issues, leaving to the complaining party the burden of proof when the question is intermodal or intramodal competition, and that certainly is a measure of relief, if it were needed.

The more relevant question for your purposes it seems to me has to do with the competitive access rules.

That was a sharply contested proceeding. There are parties, such as my colleague, who believe that the roles did not go far enough. There are others who believe that they went too far.

I think what one can say is that they commanded very widespread support in both the shipping community and the railroad community, although by no means unanimous.

Now what they do I think is interesting to note. First of all, they provide for a procedure for notice and negotiation if it——

Senator SPECTER. I wonder if I might interrupt you for just a moment, please. I am sorry for the interruption, but we are in the middle of a markup of an appropriations bill and I regret that I cannot stay longer, but I would like the record to show that I will be submitting questions for the record, and I very much regret the interruption.

Senator DeConcini. Is the Senator from Pennsylvania going back to the Appropriations Committee?

Senator Specter. Yes.

Senator DeConcini. Would the Senator from Pennsylvania be kind enough to advise the chairman of the Interior Committee that I have an amendment that I would like to offer before he closes that chapter.

Senator Specter. I will advise him, if he is there. He was not, when I left. We are on agriculture. But I will see to it that he is so advised prior to your return, Senator DeConcini.

Senator DeConcini. I would be most indebted to the Senator from Pennsylvania.

Senator Specter. Again, my apologies. Thank you, Senator.

Senator DeConcini. Thank you. Go ahead, Mr. Dempsey.

Mr. Dempsey. They provide a procedure for notice and consultation, and then—and this is a major concession that the railroads made—if the proposal will result in the elimination of railroad competition, putting to one side other competition, they will be suspended, the action will be suspended and investigated.

In reaching the merits, the Commission will not consider product competition at all, and if geographic competition is alleged, the railroad has the burden of proof. The shipper retains the burden of proof as to intermodel and intramodal competition. The fundamental standard to be applied is whether or not the proposed action is necessary to promote the competitive policies of the Staggers Act, or, looking at it differently, whether the proposed action would infringe the competitive policies of the Staggers Act.

Now, I have to agree that that is a general standard. We in effect offered the NIT League the option of writing the Sherman Act standards into these regulations, and they declined, for reasons that they thought were good and sufficient. Those standards would have been somewhat more specific.

Now I think all that one can say now is that, while the standard is appropriate, there is disagreement on exactly how the Commission will interpret it. As to that, I think all that one can say is we are just going to have to wait and see, and I do not suppose everyone will be satisfied. They cannot be.

Senator DeConcini. Mr. Calderwood, would you give us a brief response to Mr. Grassley's question. Also, I have a question I want to ask you as a followup.

Mr. Calderwood. OK. Well, I do not believe that the ICC is going to be effective in this for any number of reasons. They have been really futzing around since the Staggers Act was passed in 1980, with various guidelines, and rulings, and so forth, but without ever really being able to come to very many standards on this.

One of the problems we have is that the Commission, the seven current members—by operation of law in December it goes to five members—there have been disputes between them on some of these votes. There have been flip-flops, frankly, in some of these, and it has made it very, very difficult for anyone to try to get any consistent idea about how they are going to approach it.

But basically, they have refused, really, to take jurisdiction in most of these issues. I think that for many commodity categories—

that is piggyback and perishables—they mentioned their jurisdiction, by their own action, is extremely limited or nonexistent.

We have now today—I have seen studies that have said that over half the traffic moved on the railroads goes by contract—coal, wheat, other products.

And those are really subject to very little ICC regulation. Most of what the ICC has done is just on common carrier rates, and even that, they have refused to get involved. So I say the bottom line on it is that the ICC has been ineffective and will continue to be ineffective.

Senator DECONCINI. Mr. Calderwood, do you agree with Mr. Dempsey, that the courts are not up to handling these types of questions?

Mr. CALDERWOOD. No; I think that the courts certainly are up to handling it. First of all, I think we have to realize, there is not going to be some great flood of litigation here.

Simply put, the railroads have a built-in defense. If there is more than one railroad that is serving the points in question and serving the commodity in question, there is going to be a competitive situation.

If the traffic in question is one that can readily go my motor carrier, than that is going to be a defense. In other words, when they do not have a monopoly for the particular type of transportation involved, the same as if there is barge lines, or intercoastal steamships available to them.

So, in those situations where there is truly intermodal competition between the points in question for the traffic in question, that is a question of fact for the court to decide. But of course the courts are perfectly competent to decide that sort of thing.

In the essential facilities cases, those that have been in the courts since 1912, they have never required someone to provide facilities at less than cost, so they are not going to have to worry about being forced by a court to provide the below-cost service. Also, in essential facilities cases, the courts have always said, that the use of the facility cannot interfere with use by the owner.

In other words, here, the directors and the courts, under established essential facilities law, as recognized by the courts, is going to be provided in a way that does not interfere with the owning railroad's use of it.

The courts are experienced in essential facilities type cases, so there is nothing unusual about them handling it.

In addition, I think what we are going to see in these kind of cases is really bifurcated hearings. First, the courts will take the case, if they find there has been a violation, if they find that it is a monopoly that other modes are not effective, there is no other effective rail competition—if they make a finding like that, then they will proceed to the issue of remedies, and I think we would find in those situations, as we do in most essential facilities cases, that the parties then will work out a solution between themselves, that will then be accepted by the courts.

So, in general, I do not think there is going to be a major problem with the courts being able to handle the litigation.

Senator DECONCINI. Thank you, Mr. Calderwood.

Mr. WENDELIN. Would the Senator mind if I commented on that issue?

Senator DECONCINI. Let me ask you a question, first, because I am going to be called away any moment, and if I have to leave, you can comment for the record.

One very interesting proposition that you put forward is that though you are the Railroads Against Monopoly—I presume that is the "big guys", that you feel cut out of certain areas, where you think you could be competitive—and yet, your testimony goes, as I understand it, rather than proceed with this type of legislation, we ought to leave it in the ICC. Is that correct?

Mr. WENDELIN. Yes.

Senator DECONCINI. Is that a fair summary?

Mr. WENDELIN. I believe that is a fair summary and in part it goes back to the——

Senator DECONCINI. What makes you think the ICC will be fair to you, from your organization's point of view?

Mr. WENDELIN. I think the ICC will not be fair to our organization unless we undertake to take additional legislation and other directives, as I mentioned, to clarify for the ICC that in fact they should promote competition within the rail industry.

Senator DECONCINI. All right. So your proposition is similar to the bill S. 477, which I think is before the Commerce Committee. Are you familiar with that bill?

Mr. WENDELIN. I cannot say that I am very familiar with it.

Senator DECONCINI. It turns its attention toward the ICC and mandates that they make certain changes. Would you prefer that type of a legislative approach?

Mr. WENDELIN. Yes, Senator. Let me just emphasize again, that as a businessman, I am most interested in having the ability to have legislation which will allow me to respond to the marketplace today.

One of the problems we see with the particular bill before you today is that while the courts may have the ability to adjudicate these things effectively, in fact, it is only going to be useful in cases where you are involving biggest shippers with major amounts of traffic. It is well known, that in most sectors of our economy, the competitive edge is not provided by those biggest companies, it is provided by the small carriers, and the small companies, and the medium-sized companies who maybe have one plant or two plants.

Senator DECONCINI. Are you familiar with Carl L. Lyon?

Mr. WENDELIN. Yes, sir. I am.

Senator DECONCINI. He represents your organization, I believe?

Mr. WENDELIN. He represents the RAM group; yes, sir.

Senator DECONCINI. Are you familiar with the letter he wrote to Chairman Rodino, dated October 2, 1984?

Mr. WENDELIN. Yes, sir. I have seen that letter.

Senator DECONCINI. You have seen that letter. I would like to quote from that letter, one paragraph, and it says as follows:

> Since the Staggers Rail Act and with the ICC's approval, we have been effectively prevented from competing on a great many routes and a great deal of traffic because of joint rate cancellations, reciprocal switching cancellations, and other similar action by large railroads. We believe that the net effect of these actions is anticompetitive, and that they have damaged our traffic and revenue base at the very

> time that larger roads are expanding theirs, particularly at our expense. We also believe that the ICC has completely failed to protect our interests or those of the public generally in this sensitive area.

Do you agree with that statement today?

Mr. **WENDELIN.** Yes, sir. I do, particularly in reference to the ICC's misadministration of the Staggers Act.

Senator **DECONCINI.** Mr. Chairman, I ask that this be printed in the record, the letter, in full, at this time.

[The letter follows:]

LAW OFFICES
CARL V LYON
SUITE 302
1101 THIRTIETH STREET, N W
WASHINGTON, D C 20007
(202) 338-8497

October 2, 1984

Peter W. Rodino, Jr., Chairman
Subcommittee on Monopolies and
Commercial Law
Committee on the Judiciary
House of Representatives
Washington, DC 20510

Dear Mr. Chairman:

On behalf of Railroads Against Monopoly ("RAM"), I wish to thank you for this opportunity to comment on H.R. 4559, a bill that would make amendments to the Sherman Act relating to certain railroad practices. We request that these comments be entered in the record of your hearings on this bill.

RAM is a group of relatively small railroads that have been competitively injured by certain actions of large railroads and the Interstate Commerce Commission, and which is seeking to achieve solutions to these problems. A list of our members is enclosed.

So why rely on the ICC?

Generally speaking, we are Class II and small Class I railroads that are in line-haul competition with the major railroads for certain railroad traffic. However, in order to reach our markets we must also interchange traffic with the major roads on fair terms in order to serve our customers. In other words, while we compete with the larger railroads, we are also dependent upon them as joint rate partners to serve our markets.

Since the Staggers Rail Act and with the ICC's approval, we have been effectively prevented from competing on a great many routes and a great deal of traffic because of joint rate cancellations, reciprocal switching cancellations, and other similar actions by large railroads. We believe that the net effect of these actions is anticompetitive, and that they have damaged our traffic and revenue bases at the very time that larger roads are expanding theirs, partially at our expense. We also believe that the ICC has completely failed to protect either our interests or those of the public generally in this sensitive area.

The members of RAM supported enactment of the Staggers Rail Act in 1980 because we believed, along with the rest of the railroad industry and many shippers, that it was time to remove the dead hand of overregulation from the railroads. ~~We continue to believe that~~ competition should rule the transportation marketplace wherever conditions permit, and that many of the reforms of the Staggers Rail Act were overdue and should be retained. However, we think that the ICC has completely mishandled the sensitive issue of competition in railroad routing, and that the net effect has been very damaging to us and to the shipping public.

We believe that your consideration of rail competition comes at an opportune time, and foreshadows what promises to be an extensive debate on the issue in the 99th Congress. We invite your attention to the fact that RAM and other groups have proposed legislation that would improve competition in the rail industry. We have focused on restoration of competitive routes through competitive joint rate arrangements rather than the approach of H.R. 4559, since we believe this is the simplest and most effective way to achieve this goal.

We welcome your concern about railroad competition, and believe that you are focusing on one of the very important issues ~~that~~ the 99th Congress must face. We look forward to working with the members of the Committee and staff in the months ahead so that more effective railroad competition can be achieved. We believe that this was Congress' intent when it enacted the Staggers Rail Act, and that it is important that this goal be fully realized.

Sincerely,

Carl V. Lyon

Carl V. Lyon

par
Enclosure

MEMBERS OF
RAILROADS AGAINST MONOPOLY (RAM)

Bessemer & Lake Erie Railroad Company ①
(and affiliated railroads)

Grand Trunk System Railroads ②

- Central Vermont Railway Inc.
- Detroit, Toledo and Ironton Railroad Company
- Duluth, Winnipeg & Pacific Railway
- Grand Trunk Western Railroad Company

Canadian owned

Green Bay and Western Railroad Company ③

McCloud River Railroad ④

Milwaukee Railroad

Missouri-Kansas-Texas Railroad Company ⑤

Pittsburgh & Lake Erie Railroad ⑥

Soo Line Railroad Company ⑦

Now a consolidated "Soo-Milwaukee" Railroad

Some Canadian ownership also.

Senator DECONCINI. Do you want to comment on the other thing you were discussing before I interrupted you?

Mr. WENDELIN. Yes, Senator. I appreciate the opportunity to do so. I might just say that one of the problems that we have with Senate bill S. 447, and to take exception to what Mr. Calderwood said, is that we are dealing with an industry here where literally hundreds of rates are discussed and dealt with every day, and every week.

And the concept that there will be no great flood of litigation leads me to believe one of two things: Either this legislation is only going to be effective in a very limited number of cases, in which case it is not going to solve the problem, or, in fact, Mr. Calderwood's viewpoint is not going to be correct, and there will be a large amount of litigation which will tend to not bode very well for the ideal of rapid adjudication, which we clearly need.

Again, we need a solution that allows the business people in this industry to respond to the marketplace on an everyday basis, and we still believe that that can be best achieved by setting the ICC on a procompetitive course, to promote interrailroad competition.

Senator DECONCINI. Thank you. Mr. Dempsey, I have a number of questions, but due to time, I am going to submit all of them. Except let me ask you this one. You cite the Energy Department's study on coal rates, which I have not had a chance to see, but I saw the news release, or some release on the subject matter. Do you dispute the testimony given by Mr. Bagalay regarding the cost as it related to the Lower Colorado River Utility Co., that he is general counsel for, where the price fell $5 a ton when there were two competitive railroads?

Mr. DEMPSEY. No. I do not dispute it. I do not know the facts there, but I assume he is reporting them accurately, and I may say that that is not unique to his situation. After the Powder River basin was opened up to competition, rates in other places fell as well, with contracts.

Senator DECONCINI. Is that not good for our system?

Mr. DEMPSEY. Well, what it shows me—excuse me—is what I think everyone is familiar with if you fly an airplane. I am going out to Minnesota this Friday, paying $200 for a round trip fare. The ordinary coach fare is $500. There are all kinds of conditions attached to this transportation that I am buying, and they are attached to it for a very good reason. I just saw on television that the air fare from New York to Norfolk is four times as much as the air fare from—I have forgotten—Louisville to Cincinnati, a comparable distance.

It has nothing to do with cost, it has everything to do with the market, and so it is conceding nothing, I think, for me to say that in the railroad industry, as in every other industry, market power is a determinant of price level, or rate level. The question, it seems to me, in the end, is whether or not the rate that is challenged is, in an absolute sense, too high.

Does it extract monopoly profits, as Mr. Calderwood said? And within that range of reasonableness, there are all kinds of gradations.

Senator DECONCINI. Well, would you agree with our witness, Mr. Fogarty, that hundreds of thousands of acres of potatoes should have stayed in the ground because there was no competition to transport the potatoes to the east coast? Is that not unreasonable, just given as a hypothetical, assuming that that is correct?

Mr. **Dempsey**. Well, if one assumes that it is correct, then it is a bad situation. I do not assume that it is, though.

Senator **DeConcini**. Well, let us assume, just for purposes of discussion, that he is accurate on what happened. Does that not demand that Congress do something to, as Mr. Wendelin says, change, or direct, or mandate, or alter the ICC, or do something like that?

Mr. **Dempsey**. Well, the one thing that is not hypothetial about it is that that rate level was 162 percent of variable cost. That is a low rate. After it was escalated it was 18 percent lower than the threshold that the Congress established in the Staggers Act.

Senator **DeConcini**. But what about your argument that the market should judge. If the market brings that rate all the way down for whatever reason, that is not consistent with the idea that the market ought to set it.

Mr. **Dempsey**. The railroad, if it is acting rationally, will set rates at levels that move traffic and at the same time, permit it to cover its variable costs and, hopefully, make some contribution to fixed costs. I am going to provide you with an answer, Senator, on that particular case.

Senator **DeConcini**. Well, yes, give me an answer on that particular case, explain whether or not you think that that is a fair situation.

Mr. **Dempsey**. Yes. But let me say, in concluding my response to that general question, I do not assume that it is in the public interest to introduce infinite competition in the rail industry any more than I do——

Senator **DeConcini**. I understand that.

Mr. **Dempsey**. Yes, because——

Senator **DeConcini**. And I really do, and——

Mr. **Dempsey**. That was as you know our northeast problem—when we had the Lehigh Valley, and the Reading, and Penn Central each taking seven cars out of a city and none of them making any money on their moves.

Senator **DeConcini**. Let me say that I appreciate you raising that, and I do not dispute that. I think that regulation is necessary here, and that is why this legislation is so carefully drawn.

Mr. **Dempsey**. Yes, sir.

Senator **DeConcini** [continuing]. And so specific, even though you may disagree with that.

Gentlemen, thank you. Your testimony has been very helpful to me. The record will remain open for 2 weeks. I have some questions, particularly for Mr. Dempsey, that I would like to submit, and also for Mr. Calderwood.

The committee will stand at recess, call of the chairman and the record will remain open for 2 weeks.

[Whereupon, at 11:44 a.m., the committee recessed, subject to the call of the Chair.]

THE RAILROAD ANTIMONOPOLY ACT OF 1985
S. 447

TUESDAY, MARCH 4, 1986

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met at 10:10 a.m., in room 226, Senate Dirksen Office Building, Hon. Strom Thurmond (chairman of the committee) presiding.

Also present: Senators DeConcini, Simpson, McConnell, Grassley, and Specter.

Staff present: Kenneth Starling, Jodi Brayton, Tara McMahon, and Alice Milder.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The CHAIRMAN. The committee will come to order.

I regret that I had to go to another committee meeting this morning for a few minutes. It was necessary that I be there and I am sorry to have delayed the hearing about 10 minutes here.

The committee is meeting today to hear further testimony on S. 447, a bill to assist rail shippers who are captive in the sense that they have access to only one rail carrier.

The bill before us would create a new antitrust violation as a means of resolving the problems said to face shippers in their dealings with railroads in the deregulated environment that now exists after passage of the Staggers Act. I understand that those same problems are also being addressed in a different way through legislation now pending in the Committee on Commerce, Science, and Transportation.

At the previous hearings of this committee, administration witnesses have opposed S. 447. The Justice Department testified that the current legal standards contained in the Sherman Antitrust Act are adequate to provide relief for shippers who are injured by monopoly railroads, and that no new violation should be created. Previous witnesses also testified that the rules and procedures of the Interstate Commerce Commission are sufficient to protect and balance the interests of both shippers and railroads.

One of the main objections raised by the Justice Department against this bill is the industry-specific antitrust rule being proposed, which goes beyond the current law. The new rule would require plaintiffs to make a lower showing to establish a violation than the current rule governing monopolization.

On the other hand, proponents of this bill complain that the Supreme Court's decision in the *Keogh* case shields ratesetting conduct of railroads from treble-damage liability. A related criticism voiced by those in favor of this bill is that the Clayton Act bars private parties from seeking court injunctions against railroads. S. 447 would remove these obstacles to private antitrust suits by shippers against railroads.

This hearing has been scheduled to supplement the record and to hear additional views on both sides of these important questions. I would invite our witnesses to provide us their views on several specific points.

First, I would ask the administration witnesses to tell us about recent changes in ICC rules and the ways in which those new rules might provide some of the relief being sought through S. 447 and the Commerce Committee bill.

Second, if the Congress enacted only those parts of this bill that now bar private suits from treble damages and injunctions, what impact would that have on competition and transportation policy. And third, I would like to learn how suits in Federal courts challenging railroad rates could be conducted and concluded in less time than ICC proceedings.

We thank these distinguished witnesses for appearing before us today and we look forward to their contribution to our deliberations on this bill.

Now our witnesses today, the first witness is the Honorable Heather Gradison, Chairman of the Interstate Commerce Commission.

Ms. Gradison, we are very pleased to have you with us. We have other witnesses here, the Honorable John H. Riley, Administrator of the Federal Railroad Administration, Department of Transportation; and for the shippers we have George Mauro, director of logistics, FMC Corp., Chicago; Dwight Long, assistant director for distribution services, ICI Americas, Inc., Wilmington, DE.

Now, we are pleased to proceed, and Ms. Gradison, you may proceed.

STATEMENT OF HEATHER J. GRADISON, CHAIRMAN, INTERSTATE COMMERCE COMMISSION, ACCOMPANIED BY JOHN HENNIGAN, CHIEF OF POLICY; DAN CAMPBELL, DEPUTY GENERAL COUNSEL; AND JANE MACKALL, DIRECTOR OF PROCEEDINGS

Mrs. Gradison. Good morning, Senator. It is good to be here. I welcome the opportunity this morning to discuss the Railroad Anti-Monopoly Act.

Before I begin my remarks, I would like to take the opportunity to introduce the folks here at the table with me. On my right is John Hennigan, Chief of Policy; on my left is Dan Campbell, our Deputy General Counsel; and on his left is Jane Mackall, Director of Proceedings.

As you can see from our testimony, the Commission does not support passage of the proposed bill. We agree with the contention that the rail industry should be competitive.

The Chairman. Speak into the microphone as much as you can, so we may hear you.

Mrs. **Gradison**. We agree with the contention that the rail industry should be competitive. And, by and large, it is. The issue is how to deal with traffic that has no short-term alternatives to rail service by one carrier.

This committee has heard a great deal of testimony about the problems faced by bulk shippers. Two points typically emerge from these statements. The first is that railroads are harming their customers through monopoly pricing. And the second is that the ICC is not exercising its intended role, that we fail to strike a balance between rail and shippers' needs. I think the best way of summarizing the Commission's testimony is to address these two contentions head-on.

It is important to remember that rail reform was undertaken because of the dire circumstances that had attended traditional regulation. The inability of the regulatory system to adjust to the emergence of motor carriers in the intercity freight market produced decades of declining earnings and investments for railroading. Rapid inflation in the 1960's and 1970's threatened to put the last nails in the coffin. Regulatory lag in adjusting prices had always had a debilitating impact on rail earnings, but, in the inflationary years just before Staggers, it became a killer. It was commonplace to consider the possibility of nationalizing the railroads, and estimates of the capital needed for revitalization, in today's dollars, would approach $25 to $30 billion.

I think you are all familiar with the circumstances I have just recounted, but I would like to restate them to make a point. Rail rates in the period before Staggers may not be much of a benchmark to decide what is or is not a reasonable rate today. If the railroads were as far behind in capital recovery as the studies suggested, something had to be wrong with pricing. It certainly would have been consistent with the pre-Staggers view to expect a substantial rise in some rates as railroads sought capital sufficiency. But talk of rising rates does not fairly characterize the post-Staggers experience.

I am not suggesting that there have not been any instances where rates have jumped dramatically. There have been a few. But from a national perspective, rates have risen only modestly above inflation for some commodities and have stayed flat or even fallen for others. The railroads, however, are in much better health today than they were in 1975, or even in 1980. Productivity gains have made the difference. New investment has made much of this productivity possible and the change in the regulatory climate has, in turn, made the new investment feasible. Putting money in the rail industry is no longer considered to be highly speculative. As long as there is no abrupt change in policy here in Washington, continued investment and continued gains in productivity are quite likely.

That is the good news. But this committee has been hearing lots of bad news. You have heard testimony from shippers that believe that they have been exposed to monopolistic abuse. How widespread and how credible are these complaints? The Commission has not undertaken any systematic, firm-by-firm study of bulk shipper experience, and given our budget and caseload, we are not in any position to do so. But others have studied that issue.

The Department of Energy has looked at coal pricing twice since Staggers, and it has twice concluded that the alarm is unfounded. The Congressional Research Service also has looked at coal prices before and after reform legislation, and the conclusion reached was, again, that rail rates were rising no faster, and maybe a little slower, than utility rates and the prices of coal at the time.

If the nonpartisan experts studying rates are not finding widespread abuse, what should you make of it when you hear, as this committee has, that rails are pricing producers right out of their markets? I think you should listen fairly critically. Captivity is a two-way street. If a product is priced out of a market, the producer earns nothing, but neither does the railroad. Railroads have every incentive to permit their customers to earn the cost of capital, because rails depend on the viability of their customer base. It is nearly impossible for a railroad to relocate its investments.

This is not to say that customer margins are never squeezed to improve rail income. But that brings me to the second major issue that I would like to discuss. As I said at the outset, supporters of S. 447 make two general points—that they are exposed to monopoly abuse, and that there is no realistic avenue for relief at the Interstate Commerce Commission. Turning to the second half of this argument, let me talk about prospects for relief at the Commission and how it works.

I will have to begin the discussion with a candid statement that until very recently the Commission did not have standards by which to decide maximum rate cases. Consequently, most of the more important rate disputes are only just now becoming ripe for decision. And, while refunds are available if rates prove to be unreasonable, it still is regrettable that this matter has dragged on for so long. It is partly a function of the complexity of prescribing rates in competitive markets, compounded by the need to make decisions in accordance with the dictates of administrative due process. We now have standards that we think are going to work, and we believe that they are based on rational economics. I am committed to giving these cases our top priority.

The most controversial aspect of our coal rate standards as now adopted is the stand alone cost test of which the Committee, I am sure, has heard a great deal. I think a lot of the criticism you heard came out of a misunderstanding, so I would like to take a minute and explain the test. It is designed to determine the current resource value of the assets being consumed and serving a group of shippers. It is another way of asking what is the least cost way to run a competing railroad. While it has frequently been characterized as the cost of building another railroad, it is not that at all. We do not include any of what economists would call barrier costs. We assume instantaneous, risk-free entry. This means that there are no construction financing costs, no uncertainty and legal expense surrounding land acquisitions, and no environmental studies or licenses, no need to amortize startup costs waiting for traffic to build—in short, nothing that would inflate the newcomer's costs above those of an existing competitor. What we get is the minimum simulated competitive entry price—minimum simulated competitive entry price. I called that a mouthful when I testified before the Senate Commerce Committee, and it still is, but that is how I would like to see the test referred to so that future misunderstandings about stand-alone-cost can be avoided.

I do not want to leave the committee with the impression that all the work on coal rate guidelines is done. We will continue to fine-tune our methodology in individual cases. We also recognize that the costs of pursuing rate cases may be too expensive and that the records too complex for small shippers or isolated movement. We intend to address these very issues in a proceeding that will be noticed shortly.

I hope the committee is also aware of the major steps the Interstate Commerce Commission has recently taken in response to criticism of our market dominance standards and competitive access standards. We have adopted new rules which shift much of the burden of showing that rates are restrained by effective competition from the shippers, who felt this was too costly and problematical, to the railroads, who agree that this task will be theirs. We have also announced that future joint rate cancellation and competitive access cases will be decided according to standards of antitrust law and the heightened concern for intrarail competition found in the national transportation policy.

Like our market dominance review, this policy change reflects an agreement struck among a number of the railroads and important shipper groups.

Last, I would like to address revenue adequacy. The Commission is unanimous in its concern with the present rules for defining revenue adequacy. We have undertaken a full review of our standards and methodology and the issue is also being considered by the GAO and the Railroad Accounting Principles Board. We expect to have at least partial results by midsummer and hope to have completed our task by fall.

If the foregoing gives you a better sense of how we are trying to regulate rail rates and access, you might still ask why will S. 447 not help? Indeed, why is it not a better way to proceed? Our testimony spells out a number of problems we see in the bill, but there is one specifically that I think deserves special attention because it runs to the very heart of the conflicts in the regulatory approach.

What the Staggers Act and the Commission's Ex Parte 347 Sub-No. 1, standards have in common is an acknowledgment that rail pricing must take demand into consideration if the end result is to be an efficient transportation system. This is so because the marginal cost of any given movement is likely to be below the real cost. Consequently, if all prices were marginally based, reasonable profitability would simply be unobtainable. Hence, in our coal rate guidelines we do not consider the marginal cost of a movement to be the competitive price. Instead, we look to demand to set the competitive price, which, we in turn, seek to restrain by limiting the recovery of that required for efficient reinvestment.

But S. 447 invites an entirely different definition of reasonable price. It assumes that the price offered by a carrier renting another's facility is competitive, and therefore reasonable. But an entering carrier's only real incentive is to increase its own marginal profitability after paying rent. If the rental payment does not reflect demand considerations for the lessor, and if the price of the new entrant is based on marginal considerations, then needed capital recovery by the lessor is unlikely and a resumption of the disinvestment of the last few decades would appear inevitable. Since we do not see how a district court could factor demand-based considerations into the determination of rental payments, we see an irreconcilable conflict between S. 447 and the principles embodied in the 1980 Staggers Rail Act.

That concludes my prepared statement and my staff and I would be happy to address any and all questions that you may have.

Thank you.

[The prepared statement of Mrs. Gradison follows:]

STATEMENT OF HEATHER J. GRADISON, CHAIRMAN
INTERSTATE COMMERCE COMMISSION
BEFORE THE SENATE COMMITTEE ON
THE JUDICIARY ON S. 447

March 4, 1986

Mr. Chairman and Members of the Committee:

I want to thank you for this opportunity to submit the views of the Commission on S. 447, a bill "to amend the Sherman Act regarding rail carriers". The Commission submitted comments to the Committee last April on an earlier version of this legislation.

S. 447 would make it unlawful for any rail carrier, with the effect of monopolizing, to deny use, on reasonable terms, of a railroad facility which is the sole facility providing rail services to a shipper. Any person injured by the owner rail carrier's violation of this new provision would be able to bring an action under section 4 of the Clayton Act (treble damages). Further, any person so injured or threatened to be injured would be allowed to bring an action for injunctive relief under section 16 of the Clayton Act.

In essence, S. 447 attempts to restrain rail rates for captive shippers by requiring a rail carrier to allow trackage rights over its lines to another carrier in order to permit that carrier access to the shipper. If the owner carrier denies use of its facilities on "reasonable" terms to another rail carrier, the owner carrier would be in violation of the Sherman Act, and would be liable for treble damages and injunctive relief under the Clayton Act.

The intent behind S. 447 is that competitive rates should be made available to captive shippers. Due to reform legislation passed in 1976 and 1980, railroads now exercise more pricing freedom than at any time in this century. This has given rise to sincere concern among shippers, particularly those that are located on the lines of a single railroad. In addition to pricing freedoms, the Staggers Rail Act of 1980 also permitted greater flexibility in restructuring joint rate divisions and joint routings. Here again, railroad actions, particularly some of the initial attempts at restructuring, gave rise to concern that isolation of shippers might become exacerbated under Staggers, and that the benefits of competitive service were being foreclosed. The Commission is aware of the importance of these concerns and agrees that price restraint is best brought about through the disciplines of competition. Nevertheless, the Commission does not support S. 447.

Our opposition is based in part on the belief that the bill creates conflicting regulatory regimes. We are also of the view that S. 447 would have a negative impact on the structure of the rail system, and that its reach is far more extensive than its authors might anticipate. The Commission has taken a number of recent actions, which will be described below, aimed at reducing the tensions over competitive access. We believe that these steps represent a solution to the access problem that is acceptable to a broad spectrum of shippers, without jeopardizing the soundness of the rail industry's economic recovery.

I would like to turn to some of the recent Commission actions aimed at balancing the concerns of shippers and railroads. I will begin with those areas that directly concern competitive access. The Commission has adopted new rules by which to decide joint rate cases and disputes involving reciprocal switching. The Commission's rules, adopted in Ex Parte No. 445 (Sub-No. 1), were the result of a negotiated agreement between the Association of American Railroads, the National Industrial Transportation League, and the Chemical Manufacturers Association. The rules provide first for extended notice of cancellations, and negotiations between affected parties. It has been our experience that many apparent problems can be solved "out of court" if there is a good faith discussion of differences. But if that fails, the rules also provide that the Commission will reach its decisions based on the principles of competitive analysis, as those principles might be understood by an antitrust court and as they are augmented by the National Transportation Policy. In other words, our analysis will take into consideration traditional competition analysis, as well as the heightened concern for inter-rail competition set out in the

National Transportation Policy. The Commission has authority to hold routings open and order reciprocal switching arrangements, and it will exercise these powers to protect shippers from isolation through anticompetitive actions.

The Commission has also not hesitated to add new competition under the construction provisions of the Interstate Commerce Act. New competition has been introduced into the Powder River Basin coal fields in Wyoming, and this has brought about enormous benefits for consumers. But it is important to recognize that this competition is feasible because the market is large enough to support more than one railroad.

Aside from competitive access issues *per se*, isolated shippers have expressed concern with the Commission's maximum rate policies, reflecting the view that isolation might have been acceptable while rates were strictly regulated, but that the Commission's existing rules offer no rate protection. Naturally, we do not agree with the notion that regulatory oversight is not available. There have been substantial difficulties in establishing a maximum rate policy under the Staggers Act. Rate regulation in the presence of competition is extremely difficult, and pre-Staggers Act attempts to use public utility models had dire consequences. We now believe that we have a suitable set of rules for maximum coal rates, and we are working to effectuate rules for other commodities, taking into account the need to provide low-cost procedures for small shippers. The delay in these matters is regrettable, though it is largely a reflection of the complexity of the problem and the necessity of complying with the standards of due process which govern our decision-making. However, the Interstate Commerce Act contains provisions for refunds where rates are shown to have been unreasonably high.

The Commission has also just undertaken a review of our revenue adequacy standards, as it has become apparent that the existing determinations do not reflect recent improvements in railroad financial performance. Finally, the Commission has revised its market dominance rules in a fashion that shifts much of the burden of proving effective competition onto the railroads. Here again, the modifications were made at the suggestion of a broad range of shippers and railroads. The result will be to minimize the cost to the shipper of this portion of a rate complaint. In short, the Commission has undertaken a wide variety of initiatives in response to criticisms of its initial implementation of the Staggers Rail Act.

But the Commission remains of the view that the reforms enacted in the Staggers Rail Act have been largely responsible for the new vigor of American railroading. These reforms include enhanced rate freedom, permitting the use of differential pricing so that rates might reflect market based considerations. Greater freedom to exit unprofitable routes and the exemption from rate regulation of many commodities and services under contract rates or by specific Commission action have also helped to eliminate many of the debilitating problems of the last decade. We now see better service at rate levels that are, on the whole, in keeping with price increases elsewhere in the economy. This coupling of improved service and price restraint has been made possible through improved productivity. Productivity has in turn come largely through enhanced investment, and the willingness to invest is traceable directly to improvement in regulatory policies. Consequently, the Commission is reluctant to endorse major changes in the regulatory scheme.

S. 447 represents a major departure from the principles underlying existing railroad regulation. The bill provides, in effect, for mandatory trackage rights for those isolated shippers who do not have the benefit of intermodal options. (It should be noted here that the Commission believes that the use of the phrase "with the effect of monopolizing" in new section 9(a) would eliminate the use of the bill's provisions where intermodal competition was effective.) This remedy for shipper isolation does not depend on the fact of any recent cancellation of a joint routing or switching arrangement. Rather, it would permit a finding of monopolization for refusal to permit trackage rights to end isolation wherever it might be found. In that sense it addresses a far greater sector of the rail customer base than that which has been affected by post-Staggers restructuring.

The practical effect of such mandatory access will be to put greater pressure on differentially-based rates, as prices will naturally decline toward marginal costs. In this context, disinvestment in fixed plant over time is certain, and the likelihood of major new investment will be diminished, although some increase in the purchase of rolling stock may occur in the short-term. Particular pressure will arise for the accelerated abandonment of light density lines. Earlier versions of S.447 assumed that a negative impact on rail investment could be forestalled by setting rental charges for trackage at "reasonable" levels. If these charges do not reflect demand, i.e., if there is a return to theories of "fully allocated costs," then recovery of joint and common costs will be impossible. Consequently, short-term gains for shippers will be eroded by a decline in the system's health and stability. And if the rental charges do reflect demand, there will have been little or no consumer gain over the existing system unless one assumes the emergence of new entry at reduced wage costs.

As noted, the Commission is also concerned that S. 447 will create competing regulatory systems. The Interstate Commerce Act is not directly amended by the bill, so there will be a duplication of remedies with individual federal courts forced to address on an ad hoc basis matters that are committed to the ICC on a national basis. Operating under a broad mandate, the Commission makes its decisions with regard to long-term considerations of the maintenance of a sound rail system. While certain Commission actions have been the object of recent criticism, we believe that Commission policy overall has permitted the revival of a reliable, private-sector rail system. It is much more difficult to imagine this outcome if each shipper-rail dispute were to be settled in separate court proceedings. Likewise, through the proceedings noted above, the

Commission is now exercising its broad mandate to make adjustments to a whole range of regulatory policies. Our purpose is to reflect in these policies the experience gained to date under the Staggers Act. Again, this type of coordinated effort would be impossible in the context of individual litigation. If national policy is to continue to include broad regulatory oversight, antitrust litigation must be limited so as to be available only where it assists in achieving that policy. That is the time-honored outcome of the doctrine of primary jurisdiction.

The Commission recognizes that private sector supporters of S. 447 have argued that the bill is no more than a logical step in the reduction of the scope of primary jurisdiction. That is, that the Staggers Act's greater reliance on competition to set rates necessarily requires the availability of antitrust suits to promote competitive entry; S. 447 therefore creates the opportunity for essential facility doctrine suits in the railroad sector. There is a surface appeal to this argument, but we urge the most critical analysis before it is accepted. In the first place, railroad rates are now set in an extremely competitive environment. As a result of that competition and the fact of substantial fixed and common costs, full recovery of investment is impossible in the absence of differentially-based pricing. That fact was fully recognized in the Staggers Act, and the Commission was given the authority to permit demand-based rates, along with the responsibility to prevent those rates from becoming unreasonable. The trackage rights provisions of S. 447 would erode this national policy.

We also do not view S. 447 as a necessarily logical extension of the essential facilities doctrine. While the Commission will leave to others a fuller examination of this issue, we would note two points. Unlike the situation in some applications of this doctrine, rates of return for railroads are not guaranteed. Rather, they are the result of competitive pressures throughout the product line. If income falls below necessary levels, there is no assured method for obtaining increased revenues from the customer base for necessary reinvestment, as is the case with public utility regulation. Secondly, S. 447 imposes the real risk of liability without assuring the fact of a "bad act," heretofore an essential part of a monopolization suit. As the Department of Justice indicated in an earlier response to this Committee, a monopolization finding under section 2 of the Sherman Act requires some act demonstrating that a monopolist has willfully acquired or maintained its monopoly position, as distinguished from achieving a monopoly position through superior performance. S. 447 appears to assume that such a finding will arise from the denial of trackage rights where an offer of "reasonable" rental payments has been made. But if the existing rate for services over the owning carrier's lines are within the parameters placed by the Commission on demand-based rates, and if the owning rail carrier were willing to accept (as one would suspect it would) a rental agreement that reflected that same demand-based contribution to margin, it would be inconsistent to argue that a "bad act" existed, since the railroad's pricing and the upper limit on its return would be consistent with the Interstate Commerce Act.

For the reasons stated, it is the Commission's considered view that action on S. 447 should be deferred. We invite this Committee's continued interest in the development of rail transport policy, and will be happy to keep you informed of progress in the several Commission proceedings mentioned above.

Interstate Commerce Commission
Washington, D.C. 20423

OFFICE OF THE CHAIRMAN

April 23, 1986

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Chairman Thurmond:

Enclosed please find the Commission's responses to questions submitted by Senator DeConcini with regard to the hearing before your Committee on March 6, 1986, on S. 447, the "Railroad Antimonopoly Act". These responses are submitted for inclusion in the record.

If I may provide you with any additional information, please let me know.

Sincerely,

Heather J. Gradison

Heather J. Gradison
Chairman

Enclosure

cc: Senator DeConcini

1. Why should railroads be shielded from significant parts of the antitrust laws, for instance, those provisions dealing with injunctive relief and application of the "essential facilities" doctrine?

As a general matter, the Commission is not opposed to antitrust actions that would promote the objectives of the National Transportation Policy. The Commission has joined with the Department of Justice in an *amicus curiae* brief in *Square D Company v. Niagara Frontier Tariff Bureau Inc.*, (U.S., No. 85-21), in asking the Supreme Court to overrule the *Keogh* doctrine that presently bars private antitrust suits for damages against regulated common carriers. However, the Commission opposes the elimination of the immunity from injunctive relief as proposed in S. 447. That opposition arises from a basic concern over the incompatibility of actions pursuant to S. 447 with the Commission's system of regulation and the goals of the National

Transportation Policy. We note that the Commission's suspension powers afford shippers relief similar to that provided by injunctions.

As to the extension of the "essential facilities" doctrine to rail carriers, the Commission has taken the position that this doctrine, particularly as modified in S. 447, could do substantial harm to the transportation system. We do not believe that comparing the circumstances of railroads with those of telephone systems, or electrical transmission systems, is proper without consideration of the critical fact that reasonable returns to the "hook-up" carrier in the latter two classes are typically guaranteed by local regulators. The Commission is unable to guarantee returns to the railroad sector due to the competitive nature of the traffic base. Furthermore, the Commission believes that S. 447 goes beyond existing doctrine, in that it creates a presumption that failure to match the prices of a would-be competitor is a sufficient indication of monopoly abuse. Without consideration of the reasonableness of a given rate to the owning carrier's own legitimate needs, and without considering the efficiency consequences of the offeror's rates and services, we do not believe it is possible to conclude that an owning carrier has acted in bad faith, or abused its market power. Consequently, we do not view S. 447 as a mere application of the "essential facilities" doctrine.

2. Do you favor competition or administrative regulation as the means to resolve economic issues concerning monopoly rail service? Why will administrative processes do a better job at protecting the consumer than competitive processes?

The Commission is on record in a number of prominent cases as favoring free enterprise, market-oriented solutions over administrative compulsion. Competition is an important part of the market, as is negotiation and joint venture. Preference for market-based solutions is also embodied in the National Transportation Policy, as amended by the Staggers Rail Act of 1980. Consequently, the Commission has sought to minimize administrative interference to the degree consistent with its other responsibilities.

3. Does the ICC currently have the jurisdiction to order the type of competitive access contained in the bill? Isn't it true that the ICC's jurisdiction over reciprocal switching and joint use of the terminal facilities does not include authority to grant extensive trackage rights in any context other than a merger proceeding?

The ICC does not currently have jurisdiction to order the type of competitive access contained in the bill. S. 447 proposes trackage rights remedies that could easily include very substantial mileage over mainline track, and trackage rights could be available to private carriers operating without license from the ICC. Outside of the merger context, the Commission's authority to impose the sharing of facilities is limited to switching and terminal operations. While mainline track is necessarily and explicitly a part of the Commission's authority, the Commission's discretion to include such track is secondary and dependent upon the more limited purposes of switching and terminal usage. The Commission has no authority to compel trackage rights for utilization by persons other than regulated rail carriers.

Although the Commission has limited power to order trackage rights, outside of the context of consolidation applications, we can approve only mutually agreeable trackage rights arrangements. We receive quite a number of requests for trackage rights that have been negotiated with the owning railroad. More and more of this is being done where the carriers find it mutually beneficial, and compensation is privately agreed upon. We recently issued a class exemption to streamline this activity. Ex Parte No. 282 (Sub-No. 9) Rail Consolidation Procedures -- Trackage Rights Exemption.

4. Isn't it true that since the passage of the Staggers Act the ICC has never ordered trackage rights in a context other than a merger proceeding?

The Commission has never ordered trackage rights of the kind contemplated in S. 447, in a context other than a merger proceeding, for the reason that it has no power to do so. (See Answer to question 3, above).

However, the Commission does have the authority to compel limited trackage rights in terminal areas under 49 U.S.C. 11103(a). This power to order joint terminal use includes the extension of trackage rights to a "reasonable distance" outside the terminal area. To date, this has been interpreted as up to 15 miles outside the terminal.

The Commission also has the authority to compel joint access through reciprocal switching, under 49 U.S.C. 11103(c). Although technically not trackage rights, reciprocal switching results in an outside railroad obtaining access to the shippers within a competing carrier's terminal area.

A list of all the cases since the Staggers Act involving reciprocal switching and joint use of terminal facilities is attached. The Commission has granted this relief when warranted in the past and will continue to do so.

Vice Chairman Simmons, with whom Commissioner Lamboley joins, submitted the following separate response to question No. 4:

I cannot agree that the attached case list illustrates a positive Commission record in the area of competitive access. I hope this record will improve under the rules adopted in Ex Parte No. 445 (Sub-No. 1).

Section 11103 Cases

No. 38726	Archer Daniels Midland Company v. Providence and Worcester Railroad Company Restoration of Prior Switching Arrangements (served March 8, 1983, not printed). Restoration of reciprocal switching arrangement denied.
No. 38891	Central States Enterprises, Inc. v. Seaboard Coast Line Railroad Company (served May 15, 1984, not printed). Reciprocal switching denied.
No. 38899	Maryland Port Administration - Petition to Determine Lawfulness of Switching Charges (served March 6, 1984, not printed). Defendant not shown to be market dominant; dismissed for lack of jurisdiction.
*No. 39021	Midtec Paper Corporation, et al. v. Chicago & North Western Transportation Company -- Use of Terminal Facilities and Reciprocal Switching

	Agreements (served July 17, 1985, not printed). Reciprocal switching denied. Reopened pending court approval by decision served November 14, 1985.
*No. 39176 (Sub-2)	Soo Line Railroad Co. v. Chicago and North Western Transportation Co. (served September 25, 1984, not printed). Increased reciprocal charges found reasonable; complaint dismissed. Reopened by decision served December 26, 1985. Parties are negotiating.
*No. 40021	Cargill, Inc. v. Baltimore and Ohio Railroad Co. Pending initial decision. Parties are negotiating.
*No. 40037	Cheney Lime & Cement Co. v. Seaboard System Railroad, Inc. ALJ ordered defendant to reinstate adequate rail service or to seek Commission approval to abandon line.
*No. 40046	Kansas City Power and Light Company, Et Al. v. Burlington Northern Railroad Company (pending initial decision).
*No. 40068	Shenango Inc., et al. v. Pittsburgh, Charters & Youghiogheny Ry. Co. (pending initial decision).
F.D. No. 29802	Delaware and Hudson Railway Company v. Consolidated Rail Corporation - Reciprocal Switching Agreement, 366 ICC 845 (1982); 367 ICC 718 (1983). Reciprocal switching granted.
F.D. No. 29831	Western Ky. Trucking Co., Louisville & Nashville R. Co. and Illinois Central Gulf R. Co. -- Reciprocal Switching Agreement (served May 9, 1983, not printed). Reciprocal switching granted.
*F.D. No. 29883	Universal Forest Products, Inc. v. Seaboard Coast Line Railroad -- Reciprocal Switching (served June 23, 1983, not printed). Reciprocal switching denied. Pending on petition for reconsideration.
F.D. No. 29908	Delaware & Hudson Railway Company and New York Department of Transportation - Exemption For Use of Terminal Facilities (served May 3, 1983, not printed). Reciprocal switching granted in part.
F.D. No. 30136	Universal Forest Products, Inc. v. Atchison, Topeka & Santa Fe Railway Co., et al. (served August 3, 1983, not printed). Dismissed at complainant's request.
F.D. No. 30137	Southern Pacific Transportation Co. v. Missouri Pacific Railroad Co., et al. (served August 20 and December 10, 1985, not printed). Joint use of terminal facilities granted.
F.D. No. 30269	Denver & Rio Grande Western Railroad Company v. Burlington Northern Railroad Company -- Joint Use of Terminal Facilities (served April 24, 1984, not printed). Joint use of terminal facilities granted.
F.D. No. 30498	Florida West Railroad Co. v. Seaboard System Company -- Terminal Facilities at Port Manatee, FL (served September 19, 1984, not printed). Dismissed at complainant's request.

F.D. No. 30509	Chicago, Milwaukee, St. Paul and Pacific Railroad Company, Debtor (Richard B. Ogilvie, Trustee) v. Iowa Northern Railroad Company - Use of Terminal Facilities near Nora Springs, IA (served November 21, 1984, not printed). Dismissed for lack of jurisdiction.
*F.D. No. 30759	Denver & Rio Grande Western Railroad Co. and Missouri, Kansas, Texas Railroad -- Joint Use of Terminal Facilities at Herinton, KS (pending initial decision).
I&S 9260	Consolidated Rail Corporation, Restriction of Reciprocal Switching, Pulp Paper and Coal. After ICC suspended, respondent voluntarily withdrew the proposal.

* Denotes pending case.

5. Aren't trackage rights routinely ordered in merger proceedings, without particular difficulty in determining compensation?

Trackage rights are not routinely ordered in consolidation cases; rather, trackage rights are frequently agreed to between the various rail carriers in the context of a merger. Typically, the parties agree to the terms of compensation for the use of the trackage rights, without ICC intervention. The only consolidation where trackage rights were ordered since the passage of the Staggers Act, where the parties had not agreed to the trackage rights, was the Union Pacific-Missouri Pacific combination.[1] Trackage rights were agreed to by the parties in the BN-Frisco merger,[2] the CSX consolidation,[3] and the acquisition of the Milwaukee Road by the Soo Line.[4]

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[1] Union Pacific--Control--Missouri Pacific; Western Pacific, 366 I.C.C. 459 (1982).

[2] Burlington Northern, Inc.--Control & Merger--St. L., 360 I.C.C. 788 (1980).

[3] CSX Corp.--Control--Chessie and Seaboard C.L.I., 363 I.C.C. 518 (1980).

[4] F.D. 2840 (9), Chicago, M. St. P. and Pac. R. Co.--Reorg.--Acq. by Grand Trunk Corp., et al. (not printed), served September 26, 1984.

Determining the appropriate compensation after ordering trackage rights can be difficult. The Commission has attempted to develop a balanced compensation rate for trackage rights so that owning railroads will be fairly compensated with at least constitutional minimum value, while the tenant railroads pay a rental that enables them to be competitive with the owning carrier.

6. Since the Commission only has limited jurisdiction in the area of trackage rights, isn't it a fact that the new competitive access rules adopted by the Commission almost by definition cannot result in any significant change in the status quo?

The rules adopted in Ex Parte No. 445 (Sub-No. 1) do address the problem of shipper isolation, and do so with the principles of antitrust analysis in the forefront. To understand this, it should be recalled that the Ex Parte No. 445 (Sub-No. 1) proceeding arose out of concern with the cancellation of joint rates and reciprocal switching agreements. Since shipper isolation was aggravated or potentially aggravated by these actions, the Commission has adopted a set of rules that require advance notice and negotiation of differences over proposed cancellations. And the Commission has adopted for itself a series of standards that make competitive analysis the crux of its decision-making process.

Consequently, abusive cancellations or refusals to offer joint rates that might sustain a suit under the antitrust laws would also give rise to relief at the Commission. Indeed, since the Commission's rules require that the burden of proving the existence of geographic competition is now placed on the railroads, that the Commission will not consider the existence of product competition at all, and since the Commission will also take into account the heightened sensitivity of the National Transportation Policy to the need for intra-modal competition, relief from the Commission is far more likely than relief under pure antitrust analysis.

7. If the ICC is abolished, will implementation of this legislation be essential to protect shippers from the abuse of railroad monopoly power.

No. Abolition of the ICC, as we understand to be proposed by the Office of Management and Budget, provides for the transfer of all existing railroad regulatory authority, including all provisions for shipper protection, to the Departments of Transportation and Justice.

The CHAIRMAN. Thank you, Mrs. Gradison.

Do you wish to make a statement now or later, Senator DeConcini?

OPENING STATEMENT OF SENATOR DENNIS DeCONCINI

Senator DECONCINI. Thank you, Mr. Chairman. I wish to make a statement now.

Mr. Chairman, as the sponsor together with Senators Simpson, Nickles, and Andrews of the pending legislation, I would like to thank you for your on-going interest in this bill. I might add that the House version of this bill as sponsored by Mr. Seiberling has garnered approximately 40 cosponsors and is likely to be processed later this spring by the House Judiciary Committee.

This is the fourth, Mr. Chairman, and I hope the final day of hearings on this bill. We have now heard from every conceivable type of witness, including today's witness from the administration who previously declined to testify but now has seen fit to come before the committee.

Support for the bill, of course, has come from the captive shippers community but it is also from a more general supportive constituency. Individuals and groups as diverse as the Governors of Texas and Montana, the American Public Power Association, the National Rural Electric Association, the Consumer Federation of America, W.R. Grace Co., Massey Coal, Sunkist Growers, the Fertilizer Institute, the National Association of Wheat Growers, Cryovac, trona producers and chemical companies have all endorsed S. 447. This wide array of support is reflective of the obvious—there is a problem out there for captive shippers. The railroads are gouging them and the ICC is sitting on its hands doing absolutely nothing about it. It may be making the railroads rich, but it is not doing anything good for the consumers of this country.

With the imminent demise of the ICC, even the hope that they might provide some relief to shippers will be removed. This will leave application of the antitrust laws the only remedy for shippers.

The playing field on which shippers must play has radically changed in the past few years. First, there has been a significant reduction in the number of railroads through mergers, and hence a significant reduction in rail competition. Assuming the successful competition of the sale of Conrail to Norfolk Southern and the merger of the Southern Pacific and Santa Fe, there will be only five major railroads serving the United States.

The exclusive territories of the railroads is large and our recent hearings on the Conrail sale antitrust ramifications indicated the substantial fear of a number of entities that rail mergers might well increase the number of captive shippers subject to monopolization rates.

Second, the ICC has refused to protect captive shippers from whatever rates are set by railroads. Further, it has used its authority to exempt other captive bulk shipments, such as coal for export, from its residual jurisdiction. These means higher sales price for the coal, fewer overseas sales, and another blot against our balance of trade.

Third, the administration has eliminated funding for the ICC in its fiscal year 1987 budget request. As I alluded to earlier, even if a miracle did occur and the ICC expressed some concern for active shippers, they will not be around to carry out their intentions.

Thus, we find that large bulk shippers, heavily dependent upon railroads, have no effective remedy to the imposition of rate charges way out of line with cost of those services and prospects looming larger that the situation will even get worse.

The legal remedies available to the rest of industry against abuse of economic and market power is the antitrust laws, but key aspects of the antitrust laws are not available to the captive shipper because the railroads are exempt from their application. This situation is an anomaly that cannot be permitted to continue.

Over the next few weeks I intend to press for legislation to restore to captive shippers the only remedy that might serve them in their efforts to further the competitive market system of price and rate setting in the railroad industry.

Thank you, Mr. Chairman.

The **CHAIRMAN**. Senator, I do not believe this chairman has refused to come before the committee.

Senator **DECONCINI**. That is correct.

The **CHAIRMAN**. I believe it was the previous chairman. At that time I believe he was not ready, he said, and he was working on some changes. At any rate——

Mrs. **GRADISON**. Mr. Chairman, I have a question. I listened intently to your remarks, Senator DeConcini, and I am concerned with the misstatement of fact that is pervasive throughout that statement. I am concerned because you truly believe that statement, and some of the things in there simply are not so.

The Interstate Commerce Commission is not sitting on its hands. We have progressed and put coal rate guidelines in place, and we have put competitive access standards in place. We are about to process those cases. We are just now in a position to make the decisions following the due process that we are required to follow by law in order to give these shippers an opportunity——

Senator **DECONCINI**. When was the Staggers Act passed?

Mrs. **GRADISON**. The Staggers Act was passed in 1980 and I have a list here of all the attempts that the Interstate Commerce Commission has made in order to implement legally those competitive access requirements and those coal rate guideline requirements.

We now have them in place. We now think we have something that is going to stand up in court. We think that we can provide an opportunity for your shippers to get a fair shake.

Senator DECONCINI. I wonder where you have been, Madam Chairman. Is it not true that since the passage of the Staggers Act, which you said was in 1980, the ICC has never ordered trackage rights in the context other than merger proceedings?

Mrs. GRADISON. That is not correct. We have ordered trackage rights.

Senator DECONCINI. I would like to see that, because I do not have any record that you have ordered trackage rights except in a merger proceeding.

Mrs. GRADISON. I stand corrected, my Deputy General Counsel advises me that in technical terms, my understanding of the times that we have granted it is incorrect. I know that we have granted trackage rights, but it may be under different circumstances than you are stating. But I am not going to——

Senator DECONCINI. I am not going to blame you. You were not there, but I think the record is clear that the Staggers Act has failed to give consideration to captive shippers and that is why this bill has been introduced. That is why there is support for this bill, because in this Senator's judgment the ICC has not responded to that market inequity and the problem. Maybe you are going to change it. I hope you are. However, it looks like you are going to be zeroed out and, although I am really upset with the ICC, I really do not think that is in the best interest of transportation.

Mrs. GRADISON. It has taken us a long time to put these standards in place and each attempt has resulted in additional fine-tuning of those standards, and I cannot guarantee that these are the best standards in the world, but I think that they will work and I would like an opportunity to make that attempt.

I think that the Staggers Act has resulted in the ability for shippers to have better rail service today than they have had available to them in the last 40 years. And if you open up the access across-the-board, the problem is nobody is going to reinvest in the railroads and then shippers are going to be left without any alternative for transportation.

Senator DECONCINI. Madam Chairman, you are making a judgment that you are not sure of—that no one will reinvest. Perhaps you have not heard the testimony from the past three hearings of captive shippers. They have not——

Mrs. GRADISON. I have read it.

Senator DECONCINI. They have not done well because the ICC has not granted this trackage right, which I think you have the right to do so under present law and the Staggers Act. For reasons beyond me you have failed to do so. I do not mean you personally, but the Commission has failed to do so and I wish they had not. I wish I did not have to introduce this. I do not like taking up the time——

Mrs. GRADISON. Could we provide for the record comments on your opening statement, because I——

Senator DECONCINI. I wish you would.

Mrs. GRADISON. All right.

[The aforementioned material follows:]

Interstate Commerce Commission
Washington, D.C. 20423

OFFICE OF THE CHAIRMAN

May 20, 1986

Honorable Dennis DeConcini
United States Senate
Washington, DC 20510

Dear Senator DeConcini:

I am writing to fulfill a commitment I made during our March 4 exchange in hearings to respond more fully to your criticism of the Commission's administration of the Staggers Rail Act. I would also like to take this opportunity to thank you for the diligence of your staff and their patience in continuing to listen to our concerns about several of the proposed versions of S. 447 and H.R. 1140.

At the suggestion of Chairman Thurmond, we have maintained a dialogue with your staff in the hopes of establishing three very general but essential points. First, we believe characterizing the post-Staggers period as one of widespread monopoly abuse is not consistent with any broadly-based assessment of rail prices and profits over the last several years. In my view, such a characterization can only be supported by severely debasing the safeguards contained in the legal concept of monopoly abuse, and focusing only on those individual situations where some disadvantage has given a party the incentive to come forward in the political process. A great portion of the commodity base which is generally considered by Staggers Act critics to be captive actually moves under mutually agreeable contracts and tariffs, and little or nothing is heard from these shippers. Even where an analysis is made of "squeaking wheel" situations, such as the work undertaken by the Department of Energy, abusive use of monopoly is not likely to be seen as the norm, if it is found at all.

Second, we have also sought to make it clear that the Commission recognizes and acts on its responsibility to keep the transition from regulated to market-based rail pricing free from overreaching and abuse where market dominance exists. We believe that the Commission's policies have been faithful to this responsibility. I will acknowledge the fits and starts, and occasional errors that accompany any complicated new undertaking. But in the past year, the Commission has made a number of significant changes in its regulatory policies, and further revisions are under consideration.' Proposals to revise the standards for revenue adequacy and to adopt maximum rate standards for non-coal commodities and small shippers are underway, and the Commission has announced its tentative conclusion that captive rates should be reduced automatically when the inflation index that takes them up indicates that they should also come back down.

This re-examination of Staggers administration, like the revisions in market dominance and competitive access policy achieved last year, testify to the agency's willingness to respond to criticisms of demonstrated legitimacy. But we do not share the dire vision portrayed by many of our more vocal private sector critics, and we do not believe that facts will support their shrill accusations. (I have again just read testimony from a coal industry trade association bewailing the market dominance policies of the Commission, testimony that conveniently ignores the fact that GAO could not find a single instance in which the Commission found against a coal shipper on the market dominace issue.) Perhaps we have been too reluctant about trumpeting achievements under the Staggers Rail Act; reticence may be in the nature of a collegial body responsible to competing interests. So let me depart from form for a moment. The bottom line for the first six years of Staggers has been a healthy industry, providing vastly improved service, with only modest price advancement.

This achievement would not have been possible had the Commission overreacted to every alleged grievance as the industry's reorientation under Staggers went forward. By adopting a posture of restraint, the Commission has encouraged private solutions, and these have shown themselves vastly superior to the regulated arrangements that preceded them.

The final point that we have sought to emphasize is that, given the general success of the Staggers Rail Act and the Commission's commitment to maintaining necessary oversight, a specialized treble damage remedy was unjustified and would conflict with the goals and the administration of rail policy. In common with other government agencies, our view of the first several versions of the Rail Antimonopoly Act has been that they created the legal fact of antitrust fault without the need of first demonstrating real commercial oppression. Despite the fact that this was not the probable intent of the sponsors, it seemed certain to us that the legislatively-stated elements of a new extension of the essential facilities doctrine risked, in effect, the creation of a status crime, and that, to avoid costly judgment, the railroads would have been forced to abandon the freedom to price rationally that is the hallmark of the Staggers legislation.

I recently attended a meeting with Bob Fiedler and others of the staffs of your office and Senator Simpson's, along with Chief Counsel Ken Starling and several private sector supporters of S. 447. Many of the points raised above were debated, and I know I profited and hope others did as well. It emerged during the discussion that a substantially altered version of the S. 447 bill was under consideration, one with chief emphasis on the repeal of elements of the primary jurisdiction doctrine. Naturally I am unable to speak with any authority on behalf of the Commission, or even for myself, in advance of reviewing the specifics of such a proposal. But I can say that I am encouraged by the development, particularly since I understand it to mean that a course of action would now include the traditional aspects of a monopolization suit, including the issue of market definition and the possibility of offering defenses predicated on commercial requirements, such as the need to price rationally and efficiently.

But even this possible revision does not alleviate the problem of overlapping jurisdiction. I would like to recommend that some thought be given to the substitution of actual for treble damages in the remedy provisions, since it is the trebling of damages which would otherwise skew the forum choice and the bargaining process that will characterize access negotiations. There are several factors that support use of actual damages. I would include the observations that the sole source status of many railroad connections reflects the inefficiency involved in the duplication of track, and that the vulnerability of shippers along these tracks is partially the result of past federal policy which had denied the right of contract and created the expectation of extensive ICC intercession. The Staggers Act has initiated a transitional phase in which shippers are rejuvenating their self-help abilities, at the same time that railroads are experiencing the responsibilities that come with expanded freedom to set rates. At this point a treble damage remedy might be unwise, unfair to railroads and unnecessary for shippers--considering the existence of additional access remedies and rate regulation by the Interstate Commerce Commission. There would seem to be insufficient justification for imposing the worst of both worlds on one sector, and providing the best of both for the other.

This brings me to our exchange of opening comments during the March 4 hearings. If the foregoing provides any help on most the apparent differences between us, the one point it does not address is your concern over the Administration's proposal to eliminate the ICC. The administration has not proposed to eliminate funding for railroad regulation. It has instead recommended the transfer of these functions to executive departments. I do agree, however, to your general proposition that reduced rail regulation entails as a corollary an increase in antitrust exposure. But this is a proposition that would seem to have validity in both directions: if antitrust exposure is measurably increased, the burden of regulation should be reduced. This argument has less force to it if the antitrust recovery is limited to actual damages.

Let me conclude by reiterating my gratitude for the receptiveness that you and your staff have shown to an exchange of views on this important matter of national policy. I believe the exchange has been fruitful, and I hope that we can continue that process.

Sincerely,

Heather J. Gradison

Heather J. Gradison
Chairman

cc: Chairman Strom Thurmond
Senator Charles E. Grassley
Senator Mitch McConnell
Senator Alan K. Simpson
Senator Arlen Specter

Senator DECONCINI. I am not sensitive and if I have made mistakes I will be glad to apologize, both publicly and to you personally.

Mrs. GRADISON. I do not mind being——

Senator DECONCINI. I feel very strongly about what the ICC has failed to do and that is why I am behind this bill with such vigor.

Mrs. GRADISON. I do not mind being accused of what we did wrong. It is just that we did not do all those things wrong and I would like an opportunity to——

Senator DECONCINI. I would be glad to apologize for any error on my part.

Mrs. GRADISON. I know we deviated from the normal practice of 5 or 10 minutes and I will step back into the normal procedures at this time.

Senator DECONCINI. Excuse me, Mr. Chairman. I am sorry to take so much time.

The Chairman. All right.

Did you want to make any statement on this subject? I noticed you turned to him. Did you want him to make any statement?

STATEMENT OF DON CAMPBELL

Mr. CAMPBELL. The only thing I was going to say is that trackage rights is both a term of art and a general term and in the sense of the term of art we have not imposed trackage rights. It is not all that clear that under the Staggers Act we could outside of the context of a merger. But there are also issues involving reciprocal switching, the use of terminal facilities that as a general matter are frequently thought of as terminal rights, as trackage rights, and the Commission has ordered reciprocal switching since Staggers, although——

The CHAIRMAN. Pull the mike up to your mouth and speak louder so we can all hear you.

Mr. CAMPBELL. The Commission has since the passage of the Staggers Act used its powers to order reciprocal switching, which is one form that falls under the general rubric of trackage rights.

Senator DECONCINI. Outside of mergers?

Mr. CAMPBELL. Yes.

[The aforementioned material follows:]

Reciprocal switching is another method of providing competitive rail service and is similar in effect to trackage rights.

A list of all the cases (twenty in number) since the Staggers Rail Act of 1980 involving reciprocal switching and joint use of terminal facilities is attached (Section 11103 cases). It is clear from the list that the Commission has granted this relief when warranted in the past and will continue to do so.

Section 11103 Cases

No. 38726	Archer Daniels Midland Company v. Providence and Worcester Railroad Company Restoration of Prior Switching Arrangements (served March 8, 1983, not printed). Restoration of reciprocal switching arrangement denied.
No. 38891	Central States Enterprises, Inc. v. Seaboard Coast Line Railroad Company (served May 15, 1984, not printed). Reciprocal switching denied.
No. 38899	Maryland Port Administration - Petition to Determine Lawfulness of Switching Charges (served March 6, 1984, not printed). Defendant not shown to be market dominant; dismissed for lack of jurisdiction.
*No. 39021	Midtec Paper Corporation, et al. v. Chicago & North Western Transportation Company -- Use of Terminal Facilities and Reciprocal Switching Agreements (served July 17, 1985, not printed). Reciprocal switching denied. Reopened pending court approval by decision served November 14, 1985.
*No. 39176 (Sub-2)	Soo Line Railroad Co. v. Chicago and North Western Transportation Co. (served September 25, 1984, not printed). Increased reciprocal charges found reasonable; complaint dismissed. Reopened by decision served December 26, 1985. Parties are negotiating.
*No. 40021	Cargill, Inc. v. Baltimore and Ohio Railroad Co. Pending initial decision. Parties are negotiating.
*No. 40037	Cheney Lime & Cement Co. v. Seaboard System Railroad, Inc. ALJ ordered defendant to reinstate adequate rail service or to seek Commission approval to abandon line.
*No. 40046	Kansas City Power and Light Company, Et Al. v. Burlington Northern Railroad Company (pending initial decision).
*No. 40068	Shenango Inc., et al. v. Pittsburgh, Charters & Youghiogheny Ry. Co. (pending initial decision).
F.D. No. 29802	Delaware and Hudson Railway Company v. Consolidated Rail Corporation - Reciprocal Switching Agreement, 366 ICC 845 (1982); 367 ICC 718 (1983). Reciprocal switching granted.

F.D. No. 29831	Western Ky. Trucking Co., Louisville & Nashville R. Co. and Illinois Central Gulf R. Co. -- Reciprocal Switching Agreement (served May 9, 1983, not printed). Reciprocal switching granted.
*F.D. No. 29883	Universal Forest Products, Inc. v. Seaboard Coast Line Railroad -- Reciprocal Switching (served June 23, 1983, not printed). Reciprocal switching denied. Pending on petition for reconsideration.
F.D. No. 29908	Delaware & Hudson Railway Company and New York Department of Transportation - Exemption For Use of Terminal Facilities (served May 3, 1983, not printed). Reciprocal switching granted in part.
F.D. No. 30136	Universal Forest Products, Inc. v. Atchison, Topeka & Santa Fe Railway Co., et al. (served August 3, 1983, not printed). Dismissed at complainant's request.
F.D. No. 30137	Southern Pacific Transportation Co. v. Missouri Pacific Railroad Co., et al. (served August 20 and December 10, 1985, not printed). Joint use of terminal facilities granted.
F.D. No. 30269	Denver & Rio Grande Western Railroad Company v. Burlington Northern Railroad Company -- Joint Use of Terminal Facilities (served April 24, 1984, not printed). Joint use of terminal facilities granted.
F.D. No. 30498	Florida West Railroad Co. v. Seaboard System Company -- Terminal Facilities at Port Manatee, FL (served September 19, 1984, not printed). Dismissed at complainant's request.
F.D. No. 30509	Chicago, Milwaukee, St. Paul and Pacific Railroad Company, Debtor (Richard B. Ogilvie, Trustee) v. Iowa Northern Railroad Company - Use of Terminal Facilities near Nora Springs, IA (served November 21, 1984, not printed). Dismissed for lack of jurisdiction.
*F.D. No. 30759	Denver & Rio Grande Western Railroad Co. and Missouri, Kansas, Texas Railroad -- Joint Use of Terminal Facilities at Herinton, KS (pending initial decision).
I&S 9260	Consolidated Rail Corporation, Restriction of Reciprocal Switching, Pulp Paper and Coal. After ICC suspended, respondent voluntarily withdrew the proposal.

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* Denotes pending case.

Senator DECONCINI. I would like to see a list of those, if I could.

Mr. CAMPBELL. Yes. I do not mean to leave you with the impression that there have been a lot of such cases, but there have not been a lot of such requests as well.

Senator DECONCINI. Well, could you supply us with the number of requests that you have had from captive shippers and the number that you have granted?

Mr. CAMPBELL. Yes, sir.

Senator DECONCINI. I would like to see that.

[The aforementioned material follows:]

Since the Transportation Act of 1920, the Commission has granted numerous trackage rights requests, and even imposed involuntary trackage rights as conditions to consolidations, to a railroad over a competitor's lines. These grants of trackage rights have led to expanded service to shippers. Trackage rights requests normally specify the line to be served, however not the shippers. Nor do these requests specify which, if any, shippers are captive. Hence, our data is not precise enough to be able to tell how many, if any, of these shippers who received added competitive service were captive. As previously indicated, trackage rights is only one form of competitive access available under the Interstate Commerce Act. The term is often used to embrace the various forms of access, as the benefits to the shipper are similar in all instances. The Commission has required alternative rail service to be made available in many instances. The new rules adopted in Ex Parte No. 445 (Sub-No. 1) are directed towards granting relief from anticompetitive behavior and also focus on captive shipper concerns. We are confident that existing statutory provisions regarding access and rate reasonableness, as implemented by us, will protect captive shippers from monopoly abuses.

Since the passage of the Staggers Rail Act of 1980, the number of requests for trackage rights from shippers who claim to be captive is the same list of twenty Section 11103 cases. The following is a breakdown of these requests:

Five have been granted; eight have been reopened and are pending, two have been dismissed for lack of jurisdiction; two have been dismissed at the complainant's request; one was voluntarily withdrawn by the respondent, and two were denied.

The CHAIRMAN. Senator DeConcini introduced this bill because he had not been able to get action. He said the ICC has delayed, has not cooperated, and now we have a new Chairman, a very handsome lady Chairman and maybe she is going to get results now and maybe that will satisfy him, but at the same time you can understand his position because he has tried for several years to get results and has not been able to get results.

Mrs. GRADISON. We are going to do the best we can.

The CHAIRMAN. You think you can get results or take care of this situation?

Mrs. GRADISON. I know I can.

The CHAIRMAN. Well, let us give her a chance.

Mrs. GRADISON. We are dedicated to getting these cases out of the Interstate Commerce Commission building. We are dedicated to resolving these coal rate guideline cases and I think you are going to be satisfied with the results. I am not saying that the shippers are going to win every time, but I think that they are going to receive a fair review of what they have before us.

Senator DECONCINI. Mr. Chairman, if you would yield—any offer of improvement in the slightest is going to be gratefully received by captive shippers and this Senator. For the last 4 years we have, in my judgment, seen nothing. I stand corrected if we have had a lot of trackage rights granted outside of mergers.

Second, since time is running out on us, Mr. Chairman, and there is no funding for the ICC in the President's budget, if the

Chairman has a time schedule I would be glad to consider holding back this legislation for a brief time while she attempts to resolve these problems.

Thank you, Mr. Chairman.

The CHAIRMAN. The able and distinguished Senator from Wyoming.

OPENING STATEMENT OF SENATOR ALAN K. SIMPSON

Mr. SIMPSON. Mr. Chairman, let me just make a brief comment. I want to sincerely commend you. You are amazing, how you handle the hearings that come before this Judiciary Committee and meet the needs of the majority and the minority as you do, and I know Senator DeConcini feels just as I do. You are superb.

I want to thank Senator DeConcini. He has given us a splendid effort, and when he says to you that he is going to press on, I know Dennis DeConcini and he is going to press on, I can tell you that. He is that way and I joined him as a cosponsor in this measure. I do not want that to go unnoted, because I think it is important to have to restore some badly needed competition to the railroad industry hauling of certain bulk products like coal, soda ash, chemicals, or forest products. These shippers of bulk products have become captive because they are served by one rail line which is the only feasible means of shipping their products.

And when we did the Staggers Act, deregulation, there was recognition of these captive shippers and so they wrote that in a bit, you know, they would be protected against unfair rates, so the ICC was directed to balance the interests there, a healthy railroad system was an equally important need to protect the shippers from monopolistic practices.

As to you, Heather Gradison, I just think it is great that you are where you are, as Chairman of the ICC and I have come to know you and admire you and you are going to do a tremendous job, and you are. But let me tell you, your predecessors did not. They sat on their fannies and did nothing with this issue and read into the Staggers Act some of the most bizarre reasoning. I believe the words "reasonable" and "competition" had to do with the comparison of what it would cost to build another railroad. Well, that is about the goofiest thing I have ever heard of in the ICC. It strains every bit of common sense.

So your predecessors placed terrible burdens on those who complained and this bill is to help protect captive shippers get back to the original intent. We in Wyoming are not going to lose the Union Pacific Railroad. Union Pacific is not going to leave. They are one of our finest corporate citizens, but in the trona patch they are the only way to haul something and that is not the best thing to have. We do not have appropriate trucking in that area.

So I am not out after somebody, I am just out for fairness and we have not had fairness before with the ICC and what you are telling me in this brief review shows me that you are beginning to do that and are doing that. Nobody is going to prevent the railroads from getting a fair return on their investments. It is not my bag. I am not interested in that at all. They deserve it. It simply makes them compete fairly in the marketplace and helps cut down these costs to shippers and consumers.

I hope you all pay close attention to the testimony of George Mauro, the Director of Logistics of FMC. He is going to provide you with a classic textbook example of a substantial shipper of one of the great natural resources of America. We produce most of the product in the United States and in the world in the Green River area of trona, soda ash, and what happens? There is only one railroad as the means for transporting his company's products. I hope you will listen to that. It is a tough situation and the ICC in the past has paid absolutely no heed except to say there is no problem.

I appreciate your obvious awareness to it and I will be interested, too, in hearing your administrative proposals, what you have done in trackage rights and so on, and I look forward to working with you on this issue.

Thank you, Mr. Chairman, very much.

The CHAIRMAN. Thank you, Senator.

Mrs. Gradison, if legislation required one railroad to allow another railroad to use its tracks, can you suggest how responsibility for accidents, labor assignments, emergency maintenance, and other common responsibilities might be allocated?

Mrs. GRADISON. I am going to turn that over to the Deputy General Counsel, Dan Campbell.

Mr. CAMPBELL. Senator, could you repeat the list of——

The CHAIRMAN. Yes, I will repeat the question again.

If legislation requires one railroad to allow another railroad to use its tracks, can you suggest how responsibility for accidents, labor assignments, emergency maintenance, and other common responsibilities might be allocated?

Mr. CAMPBELL. I think the real answer to that is no, I cannot. That is not to say that there are not trackage rights agreements in place today where those things have been negotiated by the parties. That is typically not something that the Commission is intimately involved in. In part, it is not intimately involved in it because trackage rights are widespread throughout the system, and it would be very difficult for the Commission to do that sort of thing.

Mrs. GRADISON. In fact, in considering mergers, we have often given the parties that gain trackage rights as a result of the merger the opportunity to negotiate those trackage rights agreements themselves. And then, if they could not reach agreement, they may come to the Commission. So we have handled it on a case-by-case basis in the past. We do not have standards in place for reviewing that.

The CHAIRMAN. Senator Simpson, do you have some questions?

Senator SIMPSON. No, Mr. Chairman. I want to hear the testimony of the witnesses. I think that there is no need to ask Mrs. Gradison questions because I think she is indicating and we will know when she furnishes the documentation what has been done, and I have no desire to light on you. It is your predecessors who have given me the pain, and so if you are doing things administratively, I want to see those things, I know Senator DeConcini will want to see these things. All we are interested in is that we have competition and fair rates when there is only one shipper down that track, and you can go through all the nuances of this other stuff and new railroads and investment, but that does not meet the test of what they need in that area. You cannot make them the loss leader on the system.

Mrs. GRADISON. Let me indicate that I am one of those predecessors, I was there and I stand behind a lot of the decisions that a majority of the Commission has made. I did address stand-alone costs in my opening remarks and I again feel that it is a definition of a hypothetical, efficient competitor. The calculations for stand-alone costs, I think, are going to work, but I think the name is just so misleading that that is the biggest problem we have with it. It does lend itself to many horror stories and I do not blame anyone in the legislative body for responding with legislation, "By God we as legislators are going to take care of this problem." I understand that and I feel that we, the Interstate Commerce Commission, are charged with the responsibility of making certain that the shippers have reasonable rates or viable alternatives for surface transportation.

As I said before, we do have the procedures in place and I think they are going to work. We would like an opportunity to use them. But I will take part of that blame, because it does fall rightly on my shoulders.

Senator SIMPSON. People never say that around here. Hopefully, you will do that.

The CHAIRMAN. Senator DeConcini, do you have any more questions?

Senator DECONCINI. Thank you, Mr. Chairman. I have a number of questions but I will not belabor asking all of them here. I will submit some of the questions if the Chairperson would be so kind to answer them. Let me ask this question: Does the ICC currently have the jurisdiction to order the type of competitive access contained in this bill?

Mrs. GRADISON. My Deputy General Counsel tells me that we do not.

Senator DECONCINI. OK. Is it not true that the ICC jurisdiction over reciprocal switching and joint use of terminal facilities does not include authority to grant extensive trackage rights? That is your position, correct?

Mrs. GRADISON. That is correct.

Senator DECONCINI. So if you wanted to do what this bill or what those of us who support this bill think needs to be done, you would have to have some legislative broadening of authority?

Mrs. GRADISON. That seems to be the case, yes.

Senator DECONCINI. Do you favor, Madam Chairman, competition or administrative regulations as a means to resolve economic issues concerning monopoly rail service as a philosophy?

Mrs. GRADISON. Competition all the way, and I think that the majority of the Commission shares that response. I also believe that the model that we have developed will simulate an efficient competitor and with that we should have the best of both worlds.

Senator DECONCINI. Since the ICC only has limited jurisdiction in the area of trackage rights, is it not a fact that the new competitive access rules adopted by the Commission almost by definition cannot result in any significant change in the status quo or the actions that the Commission either has taken or has failed to take?

Mrs. GRADISON. No, there can be some change in the status quo. Those standards and procedures deal with reciprocal switching, trackage rights, joint rate cancellations and rate prescriptions. If we have an agreement among the railroads and the shippers that can affect each one of those areas—Dan, would you like to add anything?

Mr. CAMPBELL. The initial concern over what has been termed competitive access arose out of joint rate cancellations and in the joint rate area the Commission does have sufficient authority to address those concerns. Trackage rights arose in the latter part of that context as a way of getting around the problems that we are seeing with joint rates and in the trackage rights area the Commission does not.

Senator DECONCINI. As I understand it, first you have to have a joint rate question before you. Then if you have a joint rate question before you, you can move on to trackage rights. Is that correct or did I misunderstand?

Mr. CAMPBELL. We cannot move on to trackage rights in the context of a joint rate dispute. That is where the authority is lacking.

Senator DECONCINI. That is where you lack authority?

Mr. CAMPBELL. Yes, sir.

Mrs. GRADISON. I think John would like to add something.

STATEMENT OF JOHN HENNIGAN

Mr. HENNIGAN. Senator, I would just like to add that there are numerous private sector agreements between railroads that involve trackage rights for reciprocal use that are entered into on their behalf. This is very common today. But disputes that come before the ICC with respect to these matters have been very few over the last 5 years. I would just like to point that out for the record, sir.

Senator DECONCINI. Can you give us any kind of idea how many you have had over the last 5 years?

Mr. HENNIGAN. We can certainly provide that for the record; yes, sir.

[The aforementioned follows:]

The Commission has granted exemptions for voluntary trackage rights on a case-by-case basis under 49 U.S.C. 10505 both by petition of rail carriers and on our own motion following submission of an application under section 11343. These proceedings reflect private sector agreements between railroads involving trackage rights. The following cases are not inclusive, but are representative.

Finance Docket No. 29357F, *Burlington Northern, Inc.--Trackage Rights--Union Pacific Railroad Company--Exemption Under 49 U.S.C. §10505 From 49 U.S.C. §§11343-46* (not printed), served December 5, 1980.

Finance Docket No. 29549 (Sub-No. 1), *Louisiana & Arkansas Railway Company--Exemption Under 49 U.S.C. §10505 From 49 U.S.C. §11343(a)* (not printed), served February 27, 1981.

Finance Docket No. 29579, *Golden Triangle Railroad, Burlington Northern, Inc., and Illinois Central Gulf Railroad Company--Petition for Exemption Under 49 U.S.C. §10505 From 49 U.S.C. §§10901 and 11343* (not printed), served June 26, 1981.

Finance Docket No. 29614, *Elgin, Joliet and Eastern Railway Company--Exemption Under 49 U.S.C. §10505 From 49 U.S.C. §11343* (not printed), served May 22, 1981.

Finance Docket No. 29732, *Chicago and North Western Transportation Company--Exemption Under 49 U.S.C. 10505 From 49 U.S.C. 11343* (not printed), served October 27, 1981.

Finance Docket No. 29463, *Norfolk & Western Rwy. Co.--Trackage Rights--Baltimore & Ohio Railroad Company* (not printed), served October 31, 1980.

Finance Docket No. 29732, *Chicago & North Western Transportation Company--Trackage Rights--Burlington Northern Railroad Company* (not printed), served October 27, 1981.

Finance Docket No. 29833, *Baltimore & Ohio Railroad Company--Trackage Rights--Rock Island Railroad Company* (not printed), served February 25, 1982.

Finance Docket No. 30202, *Seaboard Coast Line Railroad Co.--Trackage Rights--Southern Railway Co.* (not printed), served May 4, 1984.

Finance Docket No. 30280, *Transkentucky Transportation Railroad Inc.--Trackage Rights--Chesapeake & Ohio Railway Company* (not printed), served December 12, 1983.

Finance Docket No. 30537, *Missouri Pacific Railroad Company--Trackage Rights--Alton & Southern Rwy.* (not printed), served September 13, 1984.

Finance Docket No. 30466, *Southern Railway Company--Trackage Rights Exemption--Burlington Northern Railroad Company* (not printed), served October 26, 1984.

Finance Docket No. 30483, *Boston & Maine Corporation & Providence & Worcester Railroad Company--Exemption U.S.C. 11343* (not printed), served June 25, 1984.

Finance Docket No. 30533 and Finance Docket No. 30269, *Burlington Northern Railroad Company--Trackage Rights--Denver and Rio Grande Western Railroad Company* (not printed), served November 9, 1984.

Finance Docket No. 30559, *Genesee & Wyoming Railroad Co.--Trackage Rights Exemption--The Baltimore & Ohio Railroad Company* (not printed), served October 19, 1984.

Finance Docket No. 30561, *Conrail--Trackage Rights Exempt.--Baltimore and Ohio Railroad Company* (not printed), served December 31, 1984.

Finance Docket No. 30562, *The Baltimore and Ohio Railroad Company --Trackage Rights Exemption--Chicago, South Shore and South Bend Railroad* (not printed), served October 19, 1984.

Finance Docket No. 30563, *Burlington Northern Railroad Co.--Trackage Rights Exemption--Trustees of the C,M&STP&P Railroad Co.* (not printed), served, November 26, 1984.

Finance Docket No. 30565, *The Chesapeake & Ohio Railway Company Trackage Rights Exemption--Seaboard System RR Inc.* (not printed), served May 10, 1985.

Finance Docket No. 30584, *Burlington Northern Railroad Company--Trackage Rights Exemption--Soo Line Railroad Company, et al.* (not printed), served March 8, 1985.

Finance Docket No. 30585, *Akron & Barberton Belt Railroad Company --Exemption U.S.C. 11343--Consolidated Rail Corporation* (not printed), served November 21, 1984.

Finance Docket No. 3060F, *Missouri Pacific Railroad Company--Trackage Rights Exemption--Chicago & North Western & Indiana Railroad Co.* (not printed), served March 8, 1985.

Finance Docket No. 30619, *Southern Pacific Transportation Company Trackage Rights Exemption--Atchison, Topeka & Santa Fe Railroad Company* (not printed), served April 3, 1985.

Finance Docket No. 30646, *Illinois Central Gulf Railroad Company --Trackage Rights Exemption--Missouri Pacific Railroad Company* (not printed), served May 13, 1985.

Finance Docket No. 30656, *Consolidated Rail Corporation--Trackage Rights Exemption--Seaboard System Railroad, Inc.* (not printed), served September 25, 1985.

In a decision served April 19, 1985, in Ex Parte No. 282 (Sub-No. 9), *Railroad Consolidation Procedures--Trackage Rights Exemption*, the Commission exempted trackage rights based on a written agreement from regulation under 49 U.S.C. 11343(a)(6). The following notice of exemptions have been filed with the Commission:

Finance Docket No. 24243 (Sub-No. 1), *Missouri-Kansas-Texas Railroad--Trackage Rights--Chicago, Burlington & Quincy Railroad* (not printed), served September 5, 1985.

Finance Docket No. 25542 (Sub-No. 1), *Missouri-Kansas-Texas Railroad--Trackage Rights--Fort Worth & Denver Railroad Company* (not printed), served June 27, 1985.

Finance Docket No. 29018 (Sub-No. 1), *Missouri-Kansas-Texas Railroad--Trackage Rights--St. Louis, San Francisco Railway Company* (not printed), served September 5, 1985.

Finance Docket No. 30389 (Sub-No. 1), *Seaboard System Railroad--Trackage Rights--Southern Railway Company* (not printed), served January 9, 1986.

Finance Docket No. 30391 (Sub-No. 1), *Norfolk & Western Railway Co.--Trackage Rights--Southern Railway* (not printed), served January 9, 1986.

Finance Docket No. 30672, *Missouri-Kansas-Texas Railroad Company --Trackage Rights--Burlington Northern Railroad Company* (not printed), July 8, 1985.

Finance Docket No. 30681, *Consolidated Rail Corporation--Trackage Rights--Missouri Pacific Railroad Company* (not printed), served July 26, 1985.

Finance Docket No. 30686, *Missouri Pacific Railroad Company--Trackage Rights--Exemption--Consolidated Rail Corporation* (not printed), served July 8, 1985.

Finance Docket No. 30689, *The Chesapeake & Ohio Railway Company--Trackage Rights--Consolidated Rail Corporation* (not printed), served July 5, 1985.

Finance Docket No. 30692, *Grand Trunk Western Railroad Company--Trackage Rights--Consolidated Rail Corporation* (not printed), served July 16, 1985.

Finance Docket No. 30698, *Burlington Northern Railroad Company--Trackage Exemption--Missouri-Kansas-Texas Railroad Company* (not printed), served August 19, 1985.

Finance Docket No. 30698 (Sub-No. 1), *Burlington Northern Railroad Company--Trackage Rights--Missouri-Kansas-Texas Railroad Co-notice of Exemption* (not printed), served December 2, 1985.

Finance Docket No. 30699, *Burlington Northern Railroad Company--Trackage Rights--Missouri-Kansas-Texas Railroad Co-notice of Exemption* (not printed), served August 19, 1985.

Finance Docket No. 30701, *Consolidated Rail Corporation--Trackage Rights--The Milwaukee Road, Inc.--Notice of Exemption* (not printed), served August 23, 1985.

Finance Docket No. 30705, *Milwaukee Road--Trackage Rights--Consolidated Rail Corp.* (not printed), served August 13, 1985.

Finance Docket No. 30718, *Missouri Pacific Railroad Company--Trackage Rights--Southern Pacific Transportation Co.--Notice of Exemption* (not printed), served September 4, 1985.

Finance Docket No. 30728, *Denver & Rio Grande Western Railroad Company--Trackage Rights--Union Pacific* (not printed), served November 4, 1985.

Finance Docket No. 30730, *Delaware & Hudson Railway Company--Trackage Rights--Exemp. Baltimore & Ohio Railroad Co. & Buffalo, Rochester & Pittsburgh Railway Company--Notice of Exemption* (not printed), served October 8, 1985.

Finance Docket No. 30737, *The Baltimore & Ohio Railroad Company--Trackage Rights Exemption--Seaboard System Railroad, Inc.* (not printed), served October 22, 1985.

Finance Docket No. 30745, *Union Pacific Railroad Company--Trackage Rights--Exemption--Burlington Northern Railroad Company* (not printed), served December 3, 1985.

Finance Docket No. 30747, *Consolidated Rail Corporation--Trackage Rights--The Pocono Northeast Railway Inc.--Notice of Exemption* (not printed), served December 6, 1985.

Finance Docket No. 30749, *Missouri Pacific Railroad Company--Trackage Rights--Southern Pacific Transportation Company--Notice of Exemption* (not printed), served December 4, 1985.

Finance Docket No. 30750, *Burlington Northern Railroad Company--Trackage Rights Exemption--Southern Pacific Transportation Company* (not printed), served December 24, 1985.

Finance Docket No. 30751, *Gulf & Mississippi Railroad Corporation--Trackage Rights--Burlington Northern Railroad Company* (not printed), served December 11, 1985.

Finance Docket No. 30757, *Norfolk & Western Railway Company--Trackage Rights Exemption--Consolidated Rail Corporation* (not printed), served February 6, 1986.

Finance Docket No. 30767, *St. Louis Southwestern Railway Company--Trackage Rights--Missouri Pacific Railroad Company* (not printed), served January 28, 1986.

Finance Docket No. 30768, *St. Louis Southwestern Railway Company--Trackage Rights Exemption--Missouri Pacific Railroad Company* (not printed), served January 28, 1986.

Finance Docket No. 30769, *Elgin, Joliet, & Eastern Railroad Company--Trackage Rights--Norfolk & Western Railway Company* (not printed), served February 19, 1986.

Finance Docket No. 30770, *Consolidated Rail Corporation--Trackage Rights--Chicago & North Western Transportation Company* (not printed), served February 11, 1986.

Finance Docket No. 30771, *Burlington Northern Railroad Company--Trackage Rights--Spokane International Railroad Company* (not printed), served February 26, 1986.

Finance Docket No. 30772, Cuyahoga Valley Railway Company--Trackage Rights--Baltimore & Ohio Railroad Company (not printed), served January 31, 1986.

Finance Docket No. 30773, Elgin, Joliet & Eastern Railway Company--Trackage Rights--Baltimore & Ohio, Chicago Terminal Railroad Company (not printed), served February 13, 1986.

Finance Docket No. 30782, Burlington Northern Railroad Company--Trackage Rights Exemption Missouri-Kansas-Texas Railroad Company (not printed), served March 4, 1986.

Finance Docket No. 30790, Indiana Harbor Belt Railroad Company--Trackage Rights--The Baltimore & Ohio Railroad Company (not printed), served March 14, 1986.

Finance Docket No. 30792, Missouri Pacific Railroad Company--Trackage Rights--The Atchison, Topeka and Santa Fe Railway Company (not printed), served March 17, 1986.

Finance Docket No. 30793, Boston & Maine Corporation--Trackage Rights--Delaware & Hudson Railway Company (not printed), served March 19, 1986.

Finance Docket No. 30801, Missouri Pacific Railroad Company--Trackage Rights--Missouri-Kansas-Texas Railroad Company (not printed), served March 31, 1986.

Finance Docket No. 30810, Hillsdale County Railway Company Inc.--Trackage Rights Exemption--Norfolk & Western Railway Company (not printed), served April 22, 1986.

Senator **DeConcini**. The last question, Mr. Chairman. If the ICC is abolished, and personally, although I am awfully upset with the past actions of the ICC I would not want to see it abolished, but if it is abolished, and the President has submitted zero funding for it, and you are in nonexistence next year, isn't it safe to say that implementation of this legislation before us today would be essential to protect shippers from abuse of railroad monopoly power?

Mrs. Gradison No, sir.

Senator **DeConcini**. How would they——

Mrs. **Gradison**. The law is the law and the anticipation is that the Interstate Commerce Act would be transferred intact to the DOT and the hope is that the administrative procedures would be more efficient by having, for example, an administrator rather than a commission to implement those laws. But the law is the law and this legislation simply is not necessary to be enacted in the event—is not necessary to be enacted, period. But in the event that the Interstate Commerce Commission functions were to be transferred to the DOT, it still would not be necessary to have it enacted.

Senator **DeConcini**. In your opinion?

Mrs. **Gradison**. In my opinion.

Senator **DeConcini**. And if it were enacted, would you agree, Madam Chairman, that it would give greater authority to the ICC than it has today?

Mrs. **Gradison**. It would and it would also be very difficult to implement. I am sorry, I stand corrected. It would give the authority to the courts.

Senator **DeConcini**. To the courts.

Mrs. **Gradison**. It would give the authority to the courts and the result would be——

Senator **DeConcini**. And the courts would be final relief.

Mrs. **Gradison** [continuing]. Much longer delays than anyone ever complained about before the Interstate Commerce Commission.

Senator **DeConcini**. You are basing that on what? Do you have some facts on which to make your judgment that the delay over the last 5 years in getting results would be longer if it were in the court system?

Mrs. **Gradison**. Well, we have the procedures in place now and the courts would then be reinventing the wheel.

Senator **DeConcini**. However, from one side of this issue those procedures have not worked.

Mrs. **Gradison**. In your opinion, yes, sir, but those standards have just recently been put into place. So if you turn it over to the courts, you may be looking at another 6-year time lag while they grapple with the same issues that the Interstate Commerce Commission have been grappling with for the last 6 years.

Senator **DeConcini**. Arizona Public Power, I understand, has had a case pending for 7 years.

Mrs. **Gradison**. Seven years and it came to my desk today. It is magic how those things happen.

Senator **DeConcini**. I wonder where it has been. Do you know?

Mrs. **Gradison**. I found out.

Senator **DeConcini**. The reason I mention this is maybe it would take 7 years to go to the courts. My guess is even in the ninth circuit or in some of the crowded courts it would not take that long, even through the appeal route. I may be mistaken, but I think you underscore the tremendous problem and frustration if you have to wait 7 years for the ICC to get the case to the Chairman's decision process——

Mrs. **Gradison**. That is a long time.

Senator **DeConcini** [continuing]. And then not have the rules until most recently. I do not know about the public power service, but to me I would just as soon gone to court than to struggle through this.

Mrs. **Gradison**. Well, this did go to court and these procedures that we tried to put into place—I have a list here, I would like to submit it for the record of the commissioner's attempts to use coal rate guidelines.

Senator **DeConcini**. I would like to have it, please.

[The aforementioned follows:]

A history of the ICC's deliberations on maximum rate reasonableness and attempts to use coal rate guidelines

- Pre-mid 1970's - used rate comparisons primarily (for all commodities).
- Mid 1970's - Western coal movements just beginning. No Western coal commodity rates available to compare to a challenged rate. Eastern coal rates could not be used for comparison because movement data were not comparable.
- 1977 - Adopted Fully Allocated cost (FAC) test (using historic cost of capital) through adjudications.
- 1978
  - Changed FAC test to use current cost of capital to properly reflect 4-R Act policies.
  - Began Ex Parte No. 347 to set standards for Western coal only.
- 1979-80 - Adopted "7% solution" in a number of adjudications (7% over FAC). Rejected by court.
- 1980 - Ex Parte No. 347 renoticed to cover coal rates nationwide and to propose a new costing method (ton/ton-mile), which allocated more fixed cost to long distance, heavy-loading commodities (like coal). (Case retitled and renumbered as Sub-No. 1).
- 1980-1981
  - Ton/ton-mile approach applied in various Western coal cases. But we found that it produced distorted, unreasonable results in the East. (It would have required substantial reductions from existing rate levels that were not being challenged).
  - Non-coal case using rate comparisons reversed in court.
  - Approximately 800 Staggers Act Section 229 cases filed.

° 1981 - Ex Parte No. 347 renoticed to withdraw ton/ton-mile proposal. Concept of differential pricing adopted. Interim rules adopted providing for case-by-case approach until rulemaking completed.

° 1982 - Various cases decided by ALJ's and Commission without any real standard. Some parties asked that their cases be held up pending final decision in 347 (1).

° 1983 - 347 (Sub-No. 1) renoticed to propose Constrained Market Pricing (included stand alone cost constraint).

- NIT League filed petition for rulemaking seeking standards for non-coal commodities (Ex Parte No. 454).

° Mid 1984 - Record in 347 (1) closes.

- Oral argument held.

- Pending coal and non-coal cases formally held in abeyance.

- NIT League petition denied.

° 1985 - Final decision in 347(1) issued September 3, 1985.

- Petition to reopen and clarify received from Arkansas Power & Light (pending).

- Judicial review pending.

° 1986 - Issuance of Notice of Proposed Rulemaking, 347 (2) addressing non-coal commodities and small shippers.

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Mrs. **Gradison**. This list summarizes the various attempts the Interstate Commerce Commission has made to deal with the coal rate guideline issue, and now we believe that we have a process that is going to work. Seven years is a long time. Refunds can be made. They do not make anybody whole, but they are a start.

Senator **DeConcini**. Mr. Chairman, I have other questions. I want to thank the witness here for her candidness and assure her that my boistrousness regarding the ICC is not personal. Please forgive me if I insulted you because I would like to see you change the policies at ICC and see some really constructive changes. I am yet to be convinced that that is going to happen, and I would like to be proven wrong. However, unless something happens awfully soon or unless there is some evidence submitted here that convinces me otherwise I am going to have to be respectfully in disagreement with the Chairman.

Thank you.

Senator **McConnell** [presiding]. Thank you, Senator DeConcini. Senator Specter.

STATEMENT OF SENATOR ARLEN SPECTER

Senator **Specter**. Thank you, Mr. Chairman.

I want to commend the chairman for scheduling these important hearings. I regret that other commitments will prevent my being here very long, but I would like to submit questions for the record. This is a very important subject which we are all going to be following very closely. It has enormous impact on the Nation's transportation system and very important impact on Conrail, among other very important subjects.

I thank you, Mr. Chairman.

Senator **McConnell**. Thank you, Senator Specter.

Senator Grassley.

STATEMENT OF SENATOR CHARLES E. GRASSLEY

Senator **Grassley**. Mr. Chairman, I do not have any questions, but I do want to make a point to the committee that we have quite a problem in Iowa with captive shippers. I held a hearing, on August 29, in Waterloo, IA, on this subject. We have the testimony of many different interests just in my state on this subject, not only utilities but agriculture interest as well. I am here just to listen to broaden my base of knowledge on the subject. But I hope each one of the members of the committee will have their staff look at our printed record, as I believe there are some problems unique to the Midwest in regard to this subject that the committee should consider.

Thank you.

Senator **McConnell**. Thank you, Senator Grassley.

If that completes your tenure, Madam Chairman——

Mrs. **Gradison**. Thank you.

Senator **McConnell**. Our next witness is John Riley, the Administrator of the Federal Railroad Administration.

STATEMENT OF JOHN H. RILEY, ADMINISTRATOR, FEDERAL RAILROAD ADMINISTRATION, DEPARTMENT OF TRANSPORTATION, ACCOMPANIED BY JACK MASON, CHIEF COUNSEL; CHRIS ROONEY, DEPUTY ADMINISTRATOR; AND RICHARD CLEM, OFFICE OF ECONOMIC ANALYSIS

Mr. RILEY. Thank you very much. First, I appreciate the invitation to testify before the committee this morning to state the views of the Department of Transportation on S. 447.

I want to introduce the people who are here with me. On my right is our Chief Counsel, Jack Mason; on my left, my Deputy Administrator, Chris Rooney; and on my far left, Dick Clem, who heads our Office of Economic Analysis. Dick formerly was employed at the Interstate Commerce Commission before coming to us, so Dick has seen the issue from both sides of the street.

To put the matter in overview, it is our judgment that S. 447 alters the current system of rate regulation in ways that we believe over the long run would have a negative effect on both shippers and railroads, and for that reason the department strongly opposes the adoption of the bill.

Now, there are a number of reasons set forth in my testimony, but let me review the key ones verbally by way of overview. First, the act would subject the railroad industry to two separate and conflicting regulatory schemes, one at the ICC and one in the courts, and actually that understates the problem because with dozens of courts simultaneously developing standards on rates and on compensation it is highly likely that railroads would face conflicting requlatory standards in different parts of the single system.

Rate issues are complex and I have always believed that a professional commission is better equipped to deal with them than courts and juries, and I think in the long run there would be no winners in a system which duplicates regulation at the judicial and the administrative level.

Second, the bill threatens to recreate the problem of regulatory lag that hurt this industry so severely in the pre-Staggers era. As I recall back in my days as an LA in the Senate when we were debating the Staggers Act in 1979, one of the most persuasive arguments that was offered for the Staggers Act was the fact that the railroad industry was losing about $1 billion a year in revenues simply waiting for rate adjustments that ultimately were approved to be approved, and that was not just a railroad problem.

The railroads felt it in revenues and the shippers felt it in investment and service. If courts are put in the position of setting reasonable rates nearly across the board, as they would be in this bill, the due process of the judicial system could resuscitate that regulatory lag problem, and that is a particular concern with this piece of legislation, for several reasons.

Eighty-three percent of all rail movements in the country are defined as monopolies per se under this legislation, and all rates on those movements are susceptible to judicial review. This bill offers injunctive relief, treble damages and attorneys fees as an incentive to litigate, an incentive that was far more attractive than anything that existed under the pre-Staggers environment, and this threat of treble damages and possible criminal liability is bound to have a restraining impact on railroad rate movements, bringing back what was a billion-dollar-a-year regulatory lag problem and, to put that in perspective, the industry's total net income last year was about $780 million, and I think that is worth looking at.

Third, Mr. Chairman, I think it is very important, perhaps the most important argument, in my judgment the bill is of questionable fairness and questionable legality because it imposes remedy where there is neither a monopoly pricing nor the absence of competition.

Now, prior to S. 447 antitrust laws were not industry-specific. They were laws of general application, and antitrust policy was enforced on a case by case basis where all relevant factors were examined to determine the key question of whether monopoly power exists or whether monopoly pricing was being exercised.

This bill deviates from those principles by severing the railroad industry from the rest of the economy and establishing what is in effect a separate and unequal system of regulation for railroads.

The greatest problem in that context is that this bill would preclude, rather than encourage, consideration of all factors relevant to the question of whether competition actually exists.

By defining the sole usage of a railroad track as a monopoly per se, the bill precludes consideration of factors such as intermodal competition, product competition and geographic competition, factors that have a real world impact on market power and prices.

As an example, you could envision the case of the shipper that may be served by only one railroad, but particularly if he is a produce shipper might have three or four trucking companies that provide good, solid, effective competition to that carrier.

In a normal antitrust case, that evidence would be important and it would be admissible, but under this bill the railroad could not offer it and the court could not consider it. Where that leaves us is a situation where the bill actually precludes the court from considering many of the factors that bear most directly on the question of whether competition exists, and yet the railroads face sanction and possible criminal liability for restraining competition.

Now, under the revised bill which I have seen—I do not know that it has been introduced—sole track usage is again defined as a monopoly per se and that again eliminates consideration of these very real competitive factors in assessing the existence or absence of market power.

Now, if these factors could in fact be brought into evidence under the abuse provision of the revised bill—and we have had some debate on that, whether that would open the door for their introduction—but if they could be, it is still not going to change the outcome, because even if a railroad could demonstrate that there were perhaps trucking and barge competitors who competed vigorously and regulated the railroads' prices, the shipper's ability to produce even a single competing railroad bidder who would offer a lower price were to argue that if the shipper set up his own railroad he could underprice creates an antitrust violation—very serious consequences, treble damages and possible criminal liability.

In addition to violating fundamental fairness, I think these definitions produce absurd results. Now, the way the Staggers Act works, 180 percent of revenue to variable cost is the key regulatory threshold. Rates set at or under 180 percent are deemed to be reasonable per se, because of the fairly low return they yield to the industry. Rates above the 180-percent threshold remain regulated and are evaluated on a case by case basis by the Commission.

More than 80 percent of all rail rates fall at or below that threshold of reasonableness. In the case of coal, we ran the numbers on this yesterday, and 85 percent of all the published rates fall at or below the threshold of reasonableness and that probably overstates the situation, because we are only able to count published rates. There are 35,000 unpublished contract rates which are uniformly lower than the published rates.

Now, despite the fact that in excess of 80 percent of all rates are within the legislatively defined zone of reasonableness, this bill would make 90 percent of rail served locations monopolies per se. It would also make 83 percent of all rail traffic a monopoly per se.

So the bottom line is that the bill affords remedies without wrongs, it diverts an enormous amount of judicial time and effort into assessing remedies without wrongs. That is not to say that there are not violations of fair pricing. I am not saying that at all.

What I am saying is this bill is so broad in its definition that it restricts the courts from considering the very factors it would have to consider to reach a fair decision on that issue.

Fourth, the bill eliminates or at best deemphasizes revenue adequacy as a primary goal of the national transportation policy. That is another important issue. In the Staggers Act, Congress premised the national transportation policy on two equally significant objectives. Rate reasonableness for shippers and revenue adequacy for carriers.

S. 447 alters that balance by at least deemphasizing if not eliminating the revenue adequacy of the rail carriers as a goal of the national transportation policy. It seeks to maximize competitive options for shippers without regard to the overall financial stability of the carrier, and I think that is particularly true under the redrafted bill which seems to key rate reasonableness to a determination of whether a rate reflects effective competition, whether or not the carriers overall are revenue adequate.

We have learned from the pre-Staggers experience, I think is solid evidence, that you cannot divorce service issues from the financial strength of the industry. A financially weak industry cannot serve and it tends to serve rural shippers most poorly. I think it is very, very poor policy to eliminate or deemphasize revenue adequacy as a key consideration in the national transportation policy.

There is also a safety issue brought up by this bill, one that I will bring to the attention of this committee because I have the responsibility of enforcing the Nation's rail safety laws.

This bill would result in multiple carriers operating over tens of thousands of miles of what we call dark territory in the railroad industry. What I am referring to for this purpose is single-line track without signals, where train orders are dispatched in writing and handed to engineers, and that increase in traffic, multiple-carrier traffic over dark territory raises a real safety issue.

Whenever you get multiple carriers, and particularly the kind of inexperienced operators—a new shipper-owned railroad or the type referred to in the redrafted bill—operating in multiple sequence over dark, single-line track, they have to deal with train control difficulties and that increases the possibility of a serious accident.

The one really bad accident we had last year occurred in some what analogous circumstances, where we had a head-on collision in Broomfield, CO, on a single-track line which was unsignaled. By increasing the opportunity for human error and over reliance on this type of bill increases the chance for a recurrence of that type of accident.

Finally, I would like to at least note to the committee that the bill as drafted would in my judgment discourage differential pricing, if not eliminate it, and that hurts the carrier and the shipper. The committee well knows that in that range of reasonableness between 100 percent of variable cost where a railroad recovers no fixed costs and therefore probably will not carry the traffic, and the 180 percent which is deemed reasonable by the industry, railroad pricing varies widely from commodity to commodity, depending on different market conditions and depending on different competitive conditions. The facts that railroads can price differentially does help both the carrier and the shipper.

From the railroad's perspective, it allows the carrier to spread its fixed cost over a larger universe of shippers than it would otherwise have access to. It also enables the carrier to maximize the effective utilization of its line.

From the shipper's perspective, it makes service available to shippers who would otherwise be priced out of the market if all rates had to be set at a single percentage.

Now, S. 447 would establish a fairly rigid standard of reasonableness, particularly the original draft of the bill, which ties rates to a share of traffic on given lines, and it would discourage differential pricing.

Some rates at the upper end of the zone of reasonableness might be forced down a little bit, but there would be no net gain to shippers because rates at the bottom end of the spectrum would have to come up to compensate or the railroad would simply lose revenues, and for an industry whose overall ROI was under 5 percent again last year, that is not good news for either carrier or shipper, and the people who would be hurt the most—and, frankly, a lot of that traffic would probably be priced right off the railroads and back onto the trucks—the people who would be hurt the most by a restriction of differential pricing are the shipper groups that tend to benefit the most from it, whose returns are at the bottom of the scale, and they are grain shippers, farm and perishable product shippers and lumber shippers. They are the ones who stand to lose the most if rate adjustments at the bottom of the scale are compelled.

Mr. Chairman, the bottom line to all of this is I am not going to stand up and tell this Commission that there are not individual problems and that there are not hard cases. I have heard my share of horror stories and I have to tell you that I was impressed and encouraged by Commissioner Gradison's testimony. It really leaves me with the belief that the Commission is going to utilize the powers that it has.

But you know, in any system of regulation that depends on human beings and human judgments, there are going to be hard cases and they are going to have to be resolved on a case by case basis.

The arguments that have been raised against Staggers and the Commission are not systemic arguments. They are not the kind of arguments that justify the creation of a whole new system of regulation. They are really people arguments and they are people arguments that cannot be resolved by the creation of this type of system, and we are as committed as anybody is to addressing and resolving those hard cases.

The greatest benefit of the Staggers Act was the fact that, in addition to restoring the strength of the industry and the quality of rail service in this country, it gave shippers and carriers the incentive to solve their own problems head-to-head; 35,000 contract rates are a testimony to its success, and the history agreements between Jim Bartley and the NIT League and Bill Dempsey and the AAR are testimonies to the success of that process.

I think we take away those incentives if we throw so many of these decisions back into the courts. It is a bad policy and that is why we are opposed to this bill. But we are very concerned about the issues of captive shippers. I am pleased to see that the Commission is going to take new testimony on revenue adequacy, and we intend to be active in all those proceedings.

Thank you very much for the opportunity to testify.

[The prepared statement of Mr. Riley follows:]

TESTIMONY OF
JOHN H. RILEY
FEDERAL RAILROAD ADMINISTRATOR
U.S. DEPARTMENT OF TRANSPORTATION
BEFORE THE
COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

MARCH 4, 1986

Mr. Chairman. I appreciate the Committee's invitation to discuss the Department of Transportation's views on S. 447, the Railroad Anti-Monopoly Act. To set a context for that discussion, it is important to understand a few of the basic principles that guide railroad rate regulation today.

Railroad rates are measured as a percentage of a railroad's variable cost. Overall, a railroad must set its rates to recover between 150 and 160 percent of variable cost to break-even in an economic sense -- in other words to fully cover both fixed and variable cost and generate a reasonable rate of return. Because some traffic -- like coal -- does more damage to the track than others, and because competition from trucks and other sources at times forces rates below the break-even level, rates for different commodities will vary above or below the 160 percent level (a concept called "differential pricing").

The Staggers Rail Act established 180 percent of variable cost as the key threshold level in railroad rate regulation. In passing the Staggers Act, the Congress declared that rates set at or below the 180 percent level are reasonable _per se_. As a consequence, rates below 180 percent are deregulated. Non-exempt rates above 180 percent remain subject to Interstate Commerce Commission (ICC) regulatory authority. In challenging rates above the 180 percent level, the Commission weighs the reasonableness of the railroad's ratemaking on a case-by-case basis -- considering all relevant factors, and balancing both the shipper's right to reasonable rates and the railroad's need for adequate revenue.

More than 80 percent of all rail rates are below the 180 percent level. For coal shipments, which are lower priced because of intense source competition, more than 85 percent of the rates fell below 180 percent. These figures actually overstate average rail rates, because they do not take account of more than 35,000 unpublished contract rates, which are generally lower than published rates.

The Railroad Anti-Monopoly Act alters this balance in several ways, ways that would prove very negative to shippers and railroads over the long-run. As a consequence, the Department of Transportation strongly opposes enactment of S. 447.

The Act would subject the railroad industry to two separate and conflicting regulatory schemes.

The Act would subject the railroad industry to two conflicting regulatory schemes -- one at the ICC, and one in the courts. Because dozens of courts would be weighing rate issues against standards that are less than clear, it is highly likely that railroads would face conflicting standards in differing parts of their systems.

Railroad rate cases are complex, and courts and juries are ill-equipped to deal with them. In the long-run, there would be no winners in this system of confused and conflicting regulation.

The Act imposes remedies where neither monopoly pricing nor an absence of competition exits.

S. 447 is of questionable fairness -- and questionable legality -- because it imposes remedies -- and exposes carriers to civil and criminal liability -- in cases where there is clearly neither monopoly pricing nor an absence of competition.

Prior to this bill, antitrust laws were not industry specific. Antitrust policy is premised on a case-by-case examination of all factors relevant to the question of whether monopoly power existed, and whether it was in fact being exercised.

This bill departs from those principles by severing the railroad industry from the rest of the economy, and establishing a set of more stringent requirements that would leave the industry both separate and unequal.

More serious is the fact that it would preclude rather than encourage the consideration of all factors relevant to the question of whether competition actually exists. By defining sole usage of a railroad track as a monopoly per se, the bill precludes consideration of intermodal competition, product competition, and geographic competition -- factors that have a real world impact on market power and the rates shippers' pay.

For example, a shipper served by only one railroad may have numerous truck options that compete with rail service and effectively constrain prices. In a normal antitrust case, that evidence would be important and perfectly admissible. Under this bill, a railroad could not offer it and the court could not consider it. The court would be precluded from addressing the ultimate question of competition, but the railroad would face civil and criminal penalties for restraining it. I question the wisdom of the approach, and I question its constitutionality.

In the same way, where a firm has the option of receiving the goods that it needs from a different source, at a competitive price, the rates the railroad can charge may already be effectively constrained. But the courts would be forced to ignore the competition represented by geographic alternatives.

Finally, a consumer may be able to purchase a different product that could substitute for the traffic it receives by rail. The existence of a suitable alternative at a comparable price may effectively constrain the rates a railroad can collect. But again, under this bill, a court would be barred from considering evidence on the existence of product competition.

These definitions -- in addition to violating fundamental fairness and past antitrust policy -- produce absurd results. More than 80 percent of all rail rates fall below the 180 percent level deemed reasonable *per se*. Yet the bill would define 90 percent of rail-served locations, and 83 percent of all traffic moving, as monopolies *per se*. Thus, because the bill would force the courts to focus only on the fact that a facility is served by only one railroad, it would impose civil and criminal liability in cases where competition unquestionably does exist. It affords remedies without wrongs, and diverts an enormous amount of legal resources into the provision of legal remedies where there is neither legal wrong nor economic harm.

The bill eliminates revenue adequacy as a goal of the national transportation policy.

The Congress, in the Staggers Act, premised the national transportation policy on two equally significant objectives -- reasonable rates for shippers, and adequate revenues for railroads. S. 447 alters that balance by at least de-emphasizing, and likely eliminating, revenue adequacy as a stated objective of the national transportation policy. It seeks to maximize competitive options for shippers, without regard to the overall financial stability of the carriers. The pre-Staggers experience with railroad bankruptcies and deteriorating service gives ample evidence that there can be no adequate transportation system without financially viable carriers.

The trackage rights provision will create serious safety problems wherever there is unsignalled, single line track.

S. 447 would result in multiple carriers operating over tens of thousands of miles of "dark territory," that is, single-line track without signal systems. That raises a serious safety issue. Whenever multiple carriers, particularly inexperienced operators, share unsignalled track, they encounter train control difficulties that significantly increase the possibility of serious accident. The worst accident we faced in the railroad industry last year came under precisely these circumstances, involving a head-on collision between two trains on an unsignalled single track. By increasing the opportunities for human error, S. 447 would increase the chance for a recurrence of that type of accident.

The bill would stimulate abandonment of rural, light density lines.

By weakening railroads' cash flows, S. 447 would have a negative impact on shippers situated on rural, light density lines, that are only marginally profitable today. Whether from business lost through trackage rights or revenue losses from increased regulation of rail rates, S. 447 would unquestionably reduce the rate of return for many railroads, thus reducing the revenues available to support operations and maintenance on light density branch lines. When revenues fall, railroads invariably concentrate resources on their heaviest density main lines, rather than the light density rural and agricultural branch lines. These lines were the hardest hit under pre-Staggers regulation, and they would be at least as adversely affected by this bill. That is particularly ironic, given the fact that the small commodities shippers on these lines would draw little or no benefit from its provisions.

In short, if one believes that S. 447 will have any effect, it would favor large railroads over small regional carriers, large shippers over small, and cities -- with their high shipping concentrations -- over rural areas.

S. 447 would likely discourage efficient differential pricing -- hurting railroad and shipper alike.

Railroad rates vary widely within the "zone of reasonableness" that extends below the 180 percent threshold.* That variance, known as differential pricing, is both appropriate and beneficial in most cases. It allows railroads to spread their fixed costs over the maximum amount of traffic they can capture. S. 447 as introduced would establish a rigid standard of reasonableness, tying rail rates for a particular shipment to its share of rail traffic on a line. A railroad could be prosecuted for deviating from this uniform pricing formula. The practical effect would be elimination of differential pricing. The revised version of the bill would have the same practical effect, by encouraging courts to assess rate reasonableness and impose treble damages without examining market circumstances. Ultimately, both versions would be as harmful to shippers as they are to railroads.

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* Of course, rates above 180 percent are not per se above a maximum reasonable level. The ICC simply has the authority to review rates above that level to determine whether they are reasonable.

While some rates at the upper end of the zone of reasonableness might be forced down, railroads would be forced to compensate by raising rates at the lower end of the zone of reasonableness (or allowing lost revenues to be reflected in deferred maintenance). Shippers would receive little if any net gain -- as costs are simply shifted from one group of shippers to another. Moreover, higher prices on the highly competitive traffic at the low end of the zone of reasonableness would drive some of that business off the railroads and onto trucks. That starts another vicious cycle like those of the 1940's to 1970's. With the loss of such traffic (and the associated revenues) the remaining traffic would have to bear a larger share of the carrier's overhead expense, leaving the shippers worse off than they were before.

The bill would virtually ensure the latter result for another reason. The trackage rights provision invites competing carriers to come onto another railroad's lines and "cherry-pick" the more lucrative traffic, the traffic moving at rates in the upper end of the zone of reasonableness. The new carriers could underbid the more lucrative traffic at the upper end of the zone, and ignore the lower rated traffic. By leaving existing carriers with either lower revenues on their best traffic, or access only to the less remunerative traffic, cherry-picking would force higher costs on grain shippers, lumber shippers, produce farmers, and others who now benefit from lower prices due to differential pricing.

The bill provides no basis for assessing the reasonableness of trackage rights fees or rail rates.

Determining a just and reasonable price in any market is a difficult analytical question. S. 447 affords little guidance on how such a judgment should be made, and courts are not well equipped to deal with that issue. Judges and juries simply do not have the expertise necessary to evaluate the appropriate level of rail rates or charges for trackage rights fees, and under the antitrust laws applicable to other industries, they are not involved in that sort of decision. If the bill forced the courts to rule on what a railroad should be charging for access to its line or service, in the absence of any accepted system, the railroads would be subject to a multiplicity of standards, without any assurance of coordination or consistency. Any miscalculation by the courts would lead to declining earnings, deferred maintenance, and deteriorating service. Moreover, the lack of any clear standards in the bill virtually ensures conflicting results.

S. 447 would eliminate the downward rate flexibility that benefitted shippers during the recession of 1982.

The delays and difficulties encountered by regulated railroads in adjusting rates upward during times of high demand made pre-Staggers carriers reluctant to lower rates during slack economic periods. That changed with the passage of the Staggers Rail Act, which gave railroads the ability to adjust rates upward and downward to match market conditions. As a consequence, thousands of rates were actually lowered during the recession of 1982. This downward flexibility played a key role in helping railroads -- and shippers -- survive the effects of that recession.

By returning carriers to a system in which rate adjustments are subject to protest, litigation, and delay, S. 447 would again eliminate incentives for railroads to alter their rates to match changing market conditions. This loss of downward flexibility will hurt both shippers and carriers over the long-run.

S. 447 will weaken the ability of a reregulated rail industry to compete with a deregulated trucking industry.

In areas where railroads compete head-to-head with a deregulated trucking industry the ability to make rapid -- even daily -- adjustments in rates and services is critical to effective competition. By saddling railroads with a dual system of regulation, and discouraging efficient differential pricing, the bill would make it difficult if not impossible for railroads to remain competitive with their deregulated trucking competitors for agricultural commodities, fruits and vegetables, and other truck-competitive traffic.

S. 447 would undo the progress made in getting shippers and carriers to negotiate innovative solutions to their own issues.

One of the great accomplishments of the Staggers Act lies in the encouragement it has given railroads and shippers to negotiate rate and service issues directly with one another, rather than referring them for resolution to a board of political appointees. The success of that incentive can be measured in the more than 35,000 contracts entered by railroads and shippers since 1980, as well as the historic agreements reached between the railroads and the National Industrial Transportation League on the issues of joint rates and competitive access. The bill destroys the incentive for railroads and their customers to work together to negotiate similar arangements in the future, since it will be all too easy to return to the pre-Staggers environment, and simply refer the issues to the courts for resolution. And even in rate negotiations, the threat of treble damages would hang over one side of the table.

To assess the real position of the railroads and their shippers, it is essential to bear in mind where we were six years ago, and contrast that with the industry we know today.

When the Congress was debating the Staggers Act, nearly one-quarter of the nation's track was in bankruptcy reorganization. The relatively prosperous 1970's had witnessed the failure of 9 major carriers, coupled with a complete collapse of regional systems in the northeast and midwest. Even the strongest railroads had a tenuous hold on stability. Return on investment (ROI) industrywide hovered at about 1 or 2 percent. Because investment needs had outstripped retained earnings for eighteen of the previous twenty years, the industry faced a ten-year capital shortage in excess of $13 billion. The railroads were on their knees, and nationalization was frequently discussed as a serious policy alternative.

There were no winners under the regulatory system the Congress altered in 1980. The problems afflicting the railroads touched every rail shipper, every community served, and virtually every employee. Rural shippers were hard hit by branch line abandonments as the railroads focused their declining resources on the heaviest density lines. Poor cash flow meant deferred maintenance, which translated into car shortages, derailments, and unreliable service. Train accidents in a cash-starved industry were three times as high as they are today. In fact, the late 1970's brought a new accident category to the Federal Railroad Administration's reporting data -- the standing derailment, in which a freight car, standing perfectly still, simply fell off a track. That, believe it or not, occurred twice in a single year.

The contrast between then and now is the best testimony to the wisdom of the decisions the Congress made six years ago. Today's rail industry is healthy and profitable on an industry-wide basis. It survived the deepest recession since the 1930's without a single bankruptcy. Capital investment has increased dramatically. I cannot represent that the industry has eliminated every dollar of the $13 billion capital gap, but deferred maintenance has been virtually eliminated from the nation's main lines, and the pace of branch line abandonments has slowed. The so-called "box car shortage" evaporated when legalization of shipper contracts enabled carriers to plan the utilization of their equipment. The number of covered hopper cars is at an all-time high.

The industry's return on investment has increased fivefold to the lofty figure of 5.7 percent for 1984 -- a revealing figure, because it tells both sides of the story. This 5.7 percent is certainly a dramatic increase from the 1 to 2 percent levels of the past twenty years. But it is still less than the return an investor could receive by simply depositing money in a savings account. As the nation's utilities have argued so persuasively -- and correctly -- in their own rate cases, an industry that cannot generate a return on capital equal to the cost of borrowing is an endangered species. These ROI figures emphasize the extent, and at the same time the fragility, of the industry's recovery. The progress is real, but it can be easily eroded.

In assessing the impact of these accomplishments on national policy, it is essential to recognize that no one has gained more from the railroad's turnaround than the railroad shipper. It was only a few years ago that "railroad marketing" seemed to be a contradiction in terms. Today, price and service innovations like multiple car grain rates, just-in-time service, and reduced rate backhauls have become standard shipper benefits. Shippers have used the power to contract to lock in rates and service commitments in close to 35,000 shipper contracts. I am convinced that we have only scratched the surface of what the industry will accomplish as it becomed more accustomed to marketing in a deregulated environment.

In addition to becoming more price competitive, railroad service has become more reliable. The industry moved the record grain harvests of the last two years without the massive and costly bottlenecks that plagued shippers during the harvests of the 1970's. Agricultural equipment shortages largely disappeared after the onset of contract rates. The elimination of deferred maintenance from the nation's main lines has meant more timely and reliable service for shippers of time-sensitive commodities. Shippers have also shared in the public benefits of the Staggers Act. The industry's financial recovery has enabled the Federal government to cut its appropriations and new authorizations for rail freight assistance from $1.99 billion in fiscal year 1978 to $64 million appropriated for fiscal year 1985. And with stronger capital investment levels has come an historic improvement in railroad safety. Train accidents have been cut by two-thirds since the adoption of the Staggers Act, an improvement that tracks across every reportable accident category. As the industry's financial picture continues to solidify, these numbers will grow better.

Simple statistics make it indisputably clear that the railroads' improved financial condition has not come at the shippers' expense. Rather than simply increasing prices across the board, railroads have utilized their new-found pricing flexibility to attract a greater share of existing markets, and provide competition for commodities like perishables, for which they had been noncompetitive for decades. This base-broadening, along with more efficient equipment utilization made possible by deregulation, enabled the industry to increase its cash flows while cutting the rate of increase in rail rates by more than 50 percent.

During the 5 years preceding the Staggers Act, rail rates rose by an annual average of 10.6 percent. In the first five years after Staggers, the rate of increase has been cut to 4.6 percent. From the end of 1984 through the end of 1985, competitive pressures in a deregulated environment resulted in actual reductions in average rail rates, compared to inflation in the overall economy of close to 4 percent. And even these numbers understate deregulation's benefit to the shipper, because they primarily measure published rates -- not contract rates, which are lower and longer-term. A recent report done for the railroad industry by an independent accountant compared rates covering more than 80 percent of rail-carried grain tonnage, and found that -- when contracts are added into the equation -- grain rates have actually declined by over 25 percent since passage of the Staggers Act. Shippers of all sizes are shipping under contracts with the railroads. The benefits also spread to the farmers, as the lower charges for transportation leave more of a margin that can be paid for the grain at the farm.

Coal shippers have entered more than 1700 long-term contracts, and many utilities have cited the substantial savings they will make as a result of their ability to negotiate contracts. To assist export coal shippers at Tidewater ports, the railroads have five times voluntarily forgone the inflation adjustment they were entitled to under Staggers Act provisions. Average rail rates for coal are lower today in real terms than they were when the Staggers Act was passed. Less than 15 percent of railroads' coal traffic is even moving at rates above the 180 percent threshold. In a special study of the effects of the Staggers Act on electric utilities, the Department of Energy specifically looked into the "worst case" examples of rail rates to coal-burning powerplants and found that rail rates have not gone up unreasonably under the Staggers Act.

But perhaps the best testimony to the success of the Staggers Act lies not in what it has accomplished, but in what it has not produced. Because it is simply fact that the dire consequences feared by critics when the Act became law five years ago have not materialized. Rates did not skyrocket, even when the economy came out of the deep recession of 1982. They are rising more slowly today than at any time in the last two decades. Shortline carriers have not disappeared. Their numbers are growing at record rates, and they have prospered with the marketing flexibility made possible by the Act. The marketing choices available to shippers today are unequalled by any in the industry's history.

I have no intention of representing to the Committee that these changes, for all their benefit, came easily or painlessly. The Staggers Act changed shipping and pricing patterns that had been established for nearly a half century. There were pains of transition. There are, in fact, hard cases which must be addressed on a case-by-case basis. And the existence of the captive shipper is a reality, not a myth.

But the theme that should come through clearly from an oversight of the Staggers experience is that the railroad industry has not abused its pricing and marketing opportunities, and because of those opportunities, has become stable while providing better shipper service. It should also be clear that while no system dependent on human judgements will ever be flawless, allowing the commercial relationship between shippers and carriers to be shaped by market forces produces better results, for shippers and carriers, than a system which delegates the major share of those decisions to a board of political appointees.

Such a system creates incentives for the parties to defer, rather than resolve, the issues of greatest importance in their relationships. Placing the majority of railroad pricing decisions in the hands of the ICC imposed a slow and cumbersome process on railroads and shippers, one in which marketing is done by rate attorneys and ICC practioners. It was a process that served the shipper and the public poorly. Placing pricing decisions in the hands of the courts would have the same effect.

The Congress showed great wisdom in adopting the Staggers Act reforms six years ago. They have enabled a partially deregulated railroad industry to compete effectively with a deregulated truck industry and a largely unregulated barge industry. There have been transition pains and hard cases, as there inevitably will be in any system. But they do not imply a structural or systemic weakness in the Staggers reforms. The present regulations provide both the authority and the tools to resolve such problems on a case-by-case basis.

Senator McCONNELL. The chairman is going to be back shortly and he has a couple of questions he would like to ask you.

We have heard the concerns of shippers about actions by railroads arising from the consolidation of routes and shifts toward single-line service. Could you tell us whether these trends are the inevitable result of deregulation? Also do these trends affect some types of shippers more than others, or are they all equally affected?

Mr. RILEY. Well, I think the consolidation toward longer single-line service is actually a beneficial one to shippers, and let me say why I think that is. A railroad that offers single-line service can price its goods more efficiently then a railroad that has to do switching operations and engage in joint rates.

Almost without exception, the cost to a carrier in offering single-line service is less than the cost in offering multiple-carrier service, and I think that the decline in the increase of rail rates that followed Staggers was made possible by single-line service but it did not result from Staggers.

The changes in the structure of the industry have really resulted from the changing demographics of shipper markets and I really do not think deregulation frankly had anything to do with the consolidations. A hundred years ago, when every shipper sold what he made within 100 miles of where he lived, a network of a lot of little railroads each going about 100 miles fit shippers' needs perfectly. But as shippers expanded their markets to regional, national, then international markets, they could not afford to go give, six, and seven switching operations between the point of origin and the point of destination, and it was that expansion of the shippers' market that drove the expansion and consolidation of the railroads.

Now, single-line carriage has tended to affect—you ask a good question when you say has it affected all shippers equally. I think it has tended to affect shippers in highly concentrated markets more than it has affected shippers in isolated rural areas, frankly, but generally there is nothing inherent in that. It should affect all shippers equally. Where it does not, it is really geographics and demographics that makes the difference, but that is a good question I think.

Senator McCONNELL. The conduct of railroads became fully subject to the existing antitrust laws, not as proposed by this bill. What effect do you think that would have on national transportation policy?

Mr. RILEY. Well, it depends on how far deregulated the railroad industry is. I think that it is perfectly appropriate for a deregulated industry to be fully subjected to the scope of the antitrust laws, because you have no regulatory mechanism to address the kinds of issues that the antitrust laws address.

Where you have a regulatory system set up to handle questions of rate reasonableness, I think you have to be careful that you not create a dual structure, where on the one hand a carrier can go in and argue rate issues and get them approved by a commission and then be sued elsewhere, but that is an issue that we are looking at and we are studying to see what can be done on it.

As you probably know, the department has supported some changes in that regard in a trucking case that is now before the Supreme Court.

Senator McConnell. In the accident situation you mentioned, how would responsibility be divided between an owner railroad and a user railroad?

Mr. Riley. That is a very good question and I think it is one that is really impossible to answer. I think they would probably both be liable in a civil sense for the accident; I suspect, having been a trial lawyer for 9 years, they would each attempt to foist liability off on the other carrier.

From our perspective, we would have to enforce the operating rules on both the owner and the operating railroad. My point on that was simply this: It is certainly possible, there is nothing inherently wrong with operating two carriers under our territory, but when you do that to the extent that this bill envisions it, you create more opportunities for human error. When you create more opportunities for human error, you increase the likelihood of an accident. It is really the scale of what this bill does, more than its use in any particular situation that concerns us.

Senator McConnell. Thank you, Mr. Riley.

Mr. Riley. Thank you, Senator. I appreciate your questions.

The Chairman. Is there anything any of you wish to say now, before we move on?

Mr. Riley. Nothing other than the fact that we appreciate the thoroughness with which this committee has looked at this bill in the four hearings that it has had. And if there are any supplemental questions that the committee would like to ask, we would be glad to file written answers with the committee.

The Chairman. I think you all catch the thrust of Senator DeConcini and Senator Simpson's position and if the ICC can move on this matter and take care of it, and if there needs to be some legislation, we could provide it. These Senators have deep concerns and I feel that they can get together with the Chairman of the ICC on this matter without a long, drawn-out tough fight, because that is what it was in then.

Mr. Riley. Senator, I appreciate that comment. You know, I think the bill is premised on the assumption that the trackage rights are the only way to solve competitive issues. They are certainly a very good way, but there are other ways. There are reciprocal switching agreements, there are simply agreements between carriers.

Of the roughly 800 cases that have come up before the ICC since Staggers, it is important to note that over 760 were settled voluntarily by the parties, and that is real evidence of how effective Staggers has been in producing fair solutions.

And I agree very much—I am not necessarily in agreement with the ICC's argument, by the way, that it does not have authority to order trackage rights. I have to say that we at FRA have differed with them. We think that under several provisions they may in fact have that authority.

The Chairman. Mr. Riley, you are an expert on railroads, I wonder if you would comment here on the difference between the House bill and this bill.

Mr. RILEY. You mean the cure bill in the Senate Commerce bill and this bill?

The CHAIRMAN. Yes.

Mr. RILEY. Apropos of the comments that I made in my opening statement, this bill tries to impose two systems of regulation, one in the courts and one at the Commission, and I think that the existence of two conflicting and overlapping regulatory schemes has got to work to everybody's disadvantage.

The other bill attempts to go back and change a number of sections of the Staggers Act. I will be very candid with the chairman and say that I am not a supporter of the various proposals put forth in the cure bill. But as between the two of them, the thing that this bill does which I think is very serious and really concerns me is that, rather than just changing the regulatory system the railroad system has to like under, it subjects the industry to two systems, and one could conceivably pass both bills and subject it to two bad systems. That is my judgment on it.

The CHAIRMAN. I wonder if you could work with the Chairman of the Interstate Commerce Commission and these two Senators here and see if you cannot reach an agreement as to what is the problem, how it can best be solved in an amicable way, without having tough fights here all the way through and the House and maybe a Presidential veto and so forth. Could you do that, do you think?

Mr. RILEY. Senator, I would be glad to devote any energy that I could to that.

The CHAIRMAN. Where is the Chairman of the ICC, has she gone? Would you tell her that I wish she would work here with Mr. Riley and these two Senators to see if you all cannot get this matter adjusted.

Mr. CAMPBELL. I was very——

The CHAIRMAN. You are an attorney, and of course you have to work with them, too.

Mr. RILEY. I was impressed by the testimony of the Chairman, I have to say, and I was impressed by her energy and her dedication to that, and I would be privileged to work with her.

The CHAIRMAN. Well, she impressed me that she is now aware of this problem and she is going to solve it. Maybe she cannot solve it and we will have some legislation, I am not too sure. It may require some. So that is the reason I would like for the Chairman of the ICC and her deputy counsel and you and these Senators get together, so if you all will get together in a conference I think you can settle it.

Mr. RILEY. Thank you, Senator. I would be happy to do that.

The CHAIRMAN. Thank you very much.

[The following was subsequently supplied for the record.]

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United States Senate
COMMITTEE ON THE JUDICIARY
WASHINGTON, DC 20510

FEDERAL RAILROAD ADMINISTRATION
'86 MAR 11 AM 8 45
EXECUTIVE SECRETARIAT

March 7, 1986

Honorable John H. Riley
Administrator
Federal Railroad Administration
United States Department of Transportation
Washington, D.C. 20590

Dear John:

Following the Committee's hearing on March 4, 1986 concerning S. 447, the Railroad Antimonopoly Act, Senator Specter has requested written responses to the following questions:

> During the course of its analysis of this legislation, did the Federal Railraod Administration perform any studies relating to the impact which such legislation would have on the hundreds of thousands of rail employees in this country? Is it not true that this bill would provide for the creation of operating rights over the owning railroads' lines at lower prices, and thereby deprive employees of jobs on those lines?

Please respond to the Committee not later than the close of business on Monday, March 24, 1986. If you have any questions, please contact Ken Starling at (202) 224-8061.

With kindest regards and best wishes,

Sincerely,

Strom Thurmond

Strom Thurmond
Chairman

ST/jvb

SUPPLEMENTAL QUESTION FROM SENATOR STROM THURMOND

COMMITTEE ON THE JUDICIARY

RAILROAD ANTIMONOPOLY ACT HEARINGS

MARCH 4, 1986

TO JOHN RILEY, FEDERAL RAILROAD ADMINISTRATOR

SENATOR SPECTER: During the course of its analysis of this legislation, did the Federal Railroad Administration perform any studies relating to the impact which such legislation would have on the hundreds of thousands of rail employees in this country? Is it not true that this bill would provide for the creation of operating rights over the owning railroads' lines at lower prices, and thereby deprive employees of jobs on those lines?

MR. RILEY: I cannot quantify the effect on existing Class I employment levels, but it is clear that the legislation could have a significant impact. Under the trackage rights provision of the bill, shippers would be able to bring in other carriers that could underbid the existing railroad for the attractive traffic on the line, thus lowering volumes and revenues for the owning carrier. The owning carrier's employment requirements with respect to the line also would decline precipitously, depending on the level of traffic that remained; if the new carrier is not a Class I railroad, total employment needed to move the traffic could decline as well.

Even if the trackage rights provision were not used by the shipper, the legislation could have an impact on railroad employment levels. Because the bill assumes that the existing rate charged by the "solely serving" railroad is unreasonable, the shipper could use the threat of trackage rights, or of a court suit, to gain a lower rate, even in cases where the ICC and the Staggers Act would consider the existing rate to be reasonable. Differential pricing -- the ratemaking flexibility guaranteed in the Staggers Act that has been the key factor in turning around the industry's financial health -- would be lost. Rail revenues would decline, and employment levels along with them.

The CHAIRMAN. Now, we have some shippers here, Mr. George Mauro, director of logistics, FMC Corp., Chicago; Dwight Long, assistant director, distribution services, ICI Americas, Inc., Wilmington, DE.

If you gentlemen will come around. Now, how many of you gentlemen are going to talk on this, two of you?

STATEMENT OF DWIGHT E. LONG, ASSISTANT DIRECTOR, DISTRIBUTION SERVICES, ICI AMERICAS INC., ON BEHALF OF THE COORDINATING COMMITTEE FOR RAILROAD COMPETITION, ACCOMPANIED BY PAUL M. DONOVAN, COUNSEL; AND GEORGE T. MAURO, DIRECTOR OF LOGISTICS, FMC CORP., ACCOMPANIED BY DONALD R. KRAUSE, MANAGER, PURCHASING AND TRANSPORTATION, OWENS-ILLINOIS, INC.; AND JOHN K. MASER III, COUNSEL, AD HOC COMMITTEE ON SODA ASH TRANSPORTATION

Mr. LONG. Good morning, Mr. Chairman.

The CHAIRMAN. We will put your entire statements in the record. I guess you would like that done, do you not?

Mr. LONG. Yes, please.

The CHAIRMAN. Without objection, that will be done. Could you take about 5 minutes and give us the thrust of your statement. It is not necessary to go into a lot of detail, these are all going to be studied later.

Mr. Mauro.

Mr. LONG. With your permission, Mr. Chairman, I would like to go first. We have agreed.

The CHAIRMAN. That is fine, Mr. Long, you may proceed.

Mr. LONG. Good morning, Mr Chairman. My name is Dwight Long. I am assistant director of distribution services for ICI Americas Inc., of Wilmington, DE. In addition to presenting the views of ICI on S. 447, my remarks are endorsed by the Coordinating Committee for Railroad Competition. Accompanying me today is Paul M. Donovan, to my left, counsel for the Coordinating Committee.

You have received my prepared statement. The time allotted me this morning does not permit my addressing all of the points in that statement, but I would like to highlight a few examples of the practical problems facing ICI and similarly situated rail captive shippers, and to explain why we support S. 447 as a partial solution to those problems.

The railroad industry and its apologists have made much of the statements of economic theoreticians that there are either "no captive shippers" or "very few captive shippers." In fact, the railroad industry has gone so far as to secure the signatures of numerous eminent economists who support this view.

The theory apparently is that there are few or no captive shippers, the free market can work and is working, and there is no need for legislation such as S. 447 or any other legislation which would provide any relief for the captive shipper.

Now, all of this may be fine in the theoretical ivory towers in which theoretical economists dwell, but there is one problem for captive shippers. "It just ain't so in the real world."

In the real world, firms such as ICI, which ship heavy loading products in bulk, are indeed captive to the railroad in many, many instances. In my own thinking about captivity, I have developed three categories for handy reference to captivity. I call these legal captivity, economic captivity, and single railroad or classical monopoly captivity. There may be other types of captivity as well, but the crucial fact is we and many other shippers are captive to railroads if we want to move our products to our markets.

Let me give you some examples of situations in which ICI is captive to the rail mode. Let us start with legal capacity, because that is probably the least arguable of my three classifications.

For example, ICI produces ethylene oxide, which is a basic building block commodity chemical. We opened a worldscale ethylene oxide plant in Bayport, TX in the early 1980's. Ethylene oxide, by regulations issued by the U.S. Department of Transportation, may not move in bulk over the highways. The movement of ethylene oxide is restricted to the rail or water modes.

Now, our plant is not on the water nor to my knowledge do any of our customers have facilities for receiving ethylene oxide by water. Therefore we are truly legally captive to the rail mode when it comes to shipping this product.

ICI makes a variety of chemicals which can be called commodity chemicals because they are competitively produced by a number of other companies. With the exception of ethylene oxide, these products can legally be moved over the highways in bulk transport; however, for other than short-haul movements, the economics of tank truck transportation simply do not permit us to participate in the market.

On the other hand, most of the products do not move in large enough quantities to warrant shipping by barge, even if our customers could receive barge shipments. Since ICC has but one plant for each of these commodity chemicals, we are economically locked in or captive to the rail mode if we want to participate in distant markets.

Economists would probably say that we are not captive because we can ship by truck or barge, or because theoretically we could sell more product in the territory near our plants or for some other theoretical reason, but in the real world we sell where we can get the business and that is often in more distant markets where there is no economically practicable alternative to the rail mode. We are captive.

Finally, let me provide you with an example showing the effect of being captive to a single railroad. This example also demonstrates our concern about being captive to the rail mode on inbound as well as outbound shipments.

At our plant in Bayport, TX, one of the important raw materials we use is a flammable liquid which originates at a supplier's plant in the State of New York. We can move this material legally either by rail or in tank trucks on the highway, but we would prefer to move it by rail. We have attempted to persuade Conrail, the railroad exclusively serving the originating plant, to establish a reasonable rate for moving this product from New York to Texas, a rate that would be in line with other rates which they maintain on this and similar chemicals for equivalent distances where there is competition.

We demonstrated to Conrail that the product could be and was being moved in tank trucks at substantially lower rates. Conrail refused to establish a price even approaching, let alone meeting the direct tank truck rate, in spite of the fact that a rate at this level would provide a per mile return substantially in excess of those provided by the rates Conrail maintains on similar traffic for equivalent distances where there is competition.

Now, I can only speculate on Conrail's motives. They may be related to the fact that our shipper is located on the former Erie Railroad main line or, as it is sometimes known, the Southern Tier line across southern New York State, which Conrail has consistently attempted to downgrade or discontinue.

I do firmly believe, however, that if access to the shipping point could be secured by other railroads, we would be able to establish a reasonable rate for this product and move it directly by rail.

I could cite numerous other examples of the deleterious effects of the lack of intrarail industry competition, suffice it to say that the lack of an openly competitive market for rail transportation does impact adversely on ICI and on other captive rail shippers. This is why we support S. 447.

S. 447, if enacted with appropriate amendments, would provide a reasonably effective means of opening up access to rail captive shippers or receiving points and could thus substantially mitigate the adverse consequences of the rail captivity which we now experience.

Additionally, by exposing the rail industry to the rigors of head-to-head competition, it could be a substantial spur to producing a leaner, more efficient and more productive rail industry, with trickle-down benefits to the Nation as a whole.

The measure of the lack of intra-rail industry competition really ought not be, as some of the earlier commentators have said, what increased cost levels we as captive shippers have been exposed to, but rather the opportunities lost, the opportunities to exploit the underlying true economics of the rail industry. This can only be done if exposure to competition drives the monopoly rents out of the rail cost structure.

This bill as we support it is not a rate bill, as Administrator Riley said. It is an access bill. What we are seeking is competitive access. Competitive access and free competition could eliminate the necessity for economic regulation of the rail industry.

For these reasons, we support S. 447 and we urge your favorable consideration of it. Thank you for the opportunity to present our views.

[The prepared statement of Mr. Long follows:]

STATEMENT OF ICI AMERICAS INC.
WILMINGTON, DELAWARE

PRESENTED BY DWIGHT E. LONG

Mr. Chairman and members of the Committee on the Judiciary:

My name is Dwight E. Long. I am Assistant Director-Distribution Services for ICI Americas Inc. of Wilmington, Delaware. In addition to presenting the views of ICI Americas on Senate Bill 447, the Railroad Antimonopoly Act, I am also authorized to speak for the Coordinating Committee for Railroad Competition. Accompanying me today is Paul M. Donovan, counsel for the Coordinating Committee for Railroad Competition.

BACKGROUND AND INTERESTS OF ICI AMERICAS

ICI Americas Inc. is a wholly-owned subsidiary of Imperial Chemical Industries PLC, one of the world's largest chemical companies. ICI Americas is based in Wilmington, Delaware, and undertakes domestic production and marketing, as well as domestic and international distribution, of a wide variety of chemicals, plastics, and pharmaceuticals. When I refer to "ICI" in the balance of this statement, the reference will be to ICI Americas Inc. rather than to its parent company or other related companies.

ICI utilizes all transportation modes in the movement of raw materials to its plants and finished products from its plants to distribution centers and to customers. ICI is a significant user of railroad service and maintains a fleet of over 600 leased or owned railroad cars (tank cars or covered hoppers) to move bulk products by rail. ICI has several production plants and distribution points which are captive to one railroad and produces several products which, for reasons of either law or economics, are captive to the rail mode. Thus, ICI is vitally interested in legislation affecting railroad transportation, particularly where such legislation promises some relief for the "captive shipper."

BACKGROUND AND QUALIFICATIONS OF DWIGHT E. LONG

I have been employed by ICI since 1976, most of that time in my present position as Assistant Director-Distribution Services. Throughout all my tenure with ICI, I have been responsible for directing the acquisition of transportation services for ICI, including railroad services. My transportation career spans 25 years; almost 24 years of this have involved railroad transportation.

My undergraduate degree is in business administration with a major in transportation and a minor in economics. I have also studied business and economics subjects on the graduate level, and am currently a candidate for a J.D. degree at Delaware Law School, where I will graduate cum laude in May, 1986.

In addition to my vocational and educational experience, I have been admitted to practice before the Interstate Commerce Commission since 1964. I have been involved in numerous trade association transportation committees. Most pertinently, I served as Vice-Chairman and Chairman of the National Industrial Transportation League's Railroad Transportation Committee from 1978 through 1984 and was heavily involved in various legislative and regulatory activities carried on by the League in which the Railroad Transportation Committee, or its predecessors, played a part. I mention the latter only for background, as my remarks today are on behalf of ICI and not on behalf of the League.

THE CAPTIVITY OF ICI AS A RAIL SHIPPER

Most of the transportation services which ICI purchases or potentially could purchase from a railroad or railroads can be described as "captive traffic." This captivity arises from one of three sources: legal requirements, economic necessity, or carrier monopoly position.

Legal Captivity. The portion of the railroad transportation requirements of ICI which is legally captive consists of those products which, by law, may not move in a transportation mode (available to ICI) other than the railroad mode. ICI is a producer of ethylene oxide, a "building block" chemical commodity which is used in the production of numerous other chemicals and other products. Ethylene oxide is a flammable liquid which, by regulations promulgated by the United States Department of transportation*, may not be transported in bulk quantities via motor carriage. Although ethylene oxide can legally be transported via water carriers, the production plant of ICI is not located on a navigable waterway, nor are most of the ethylene oxide-receiving customers of ICI. In fact, I am not aware of any ICI merchant customers who have facilities for receiving ethylene oxide by water transport. Thus, all ICI shipments of ethylene oxide must move by railroad. ICI is truly a "captive shipper" in shipping ethylene oxide.

Economic Captivity. In addition to ethylene oxide, ICI ships and receives a wide variety of other commodity chemicals which move in bulk. Although these products may legally move in motor carrier transportation, as a matter of practical economics their movement via truck is restricted to short distances. The low profit margins, extremely competitive nature of the commodity chemicals business, and heavy loading nature of these products combine to make it economically unfeasible to ship them long distances by truck. Further, in many instances, the customers who receive these products are not equipped to handle trucks without additional investment in unloading facilities and are therefore reluctant, and sometimes outright refuse, to receive products shipped other than by rail. For these products, ICI is captive to the rail mode if it wishes to participate in the business. Captivity to the rail mode may not be theoretically complete, but from a practical standpoint, it is.

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* 49 C.F.R. 173.124: Since this provision contains no authorization for bulk motor carrier shipment of ethylene oxide, this mode of transport is prohibited by (intentional) omission from the Regulations.

Single Railroad Captivity. ICI also may be captive to a particular origin or destination railroad in another sense--the classical monopoly sense--where that railroad is the only railroad physically serving the shipping or receiving location and where no other railroad has access to the facility through "trackage rights" or "reciprocal switching." In such situations, ICI is "captive" to that railroad if it is forced to or wishes to use railroad transportation service. Obviously, this type of captivity can cut across both "legal captivity" and "economic captivity." It also can represent a unique captivity where neither legal or economic captivity is present, but where use of railroad transportation would be desirable, and would appear to be economic as compared with competing modes, but where the serving carrier does not deign to compete for the traffic by offering economically attractive prices, attractive service, or either. This is a sort of "reverse captivity," where the railroad is in essence making the traffic involved captive to another mode by refusing to compete on terms which reflect the underlying economic advantage of the rail mode.

Some specific examples of the captivity to the rail mode experienced by ICI may be instructive. I have already mentioned the legal captivity which the rail mode maintains over ethylene oxide shipments. These emanate from a plant at Bayport, Texas, which is served solely by the Southern Pacific Transportation Company. Therefore, in addition to legal captivity, ICI ethylene oxide shipments are also subject to single railroad captivity insofar as originations from the producing plant are concerned. For the most part, ethylene oxide destinations are also subject to single railroad captivity, in addition to the legal captivity problem. For example, ICI maintains a plant at Atlas Point, Delaware, which is a major user of ethylene oxide. This plant is served solely by Conrail. Prior to joint route-closing actions taken by Conrail, there was at least potential intra-modal competition for this business as ICI could utilize a variety of intermediate or "bridge" carriers between the originating carrier (Southern Pacific) and the delivering carrier (Conrail). After Conrail's closure of such joint rate/route combinations, the only economically feasible routing for this business is Southern Pacific-Conrail, interchanging at East St. Louis, Illinois. Both Southern Pacific and Conrail have structured the rates so as to provide themselves with the longest possible "haul" but at the expense of enabling any other railroads to compete for the business.

Products produced by ICI and originating at ICI facilities are not the only products subject to captivity. Essential raw materials used in ICI plants can also be captive. As an example, ICI uses several blends of corn syrup at its Atlas Point Plant. The corn syrup originates at non ICI-owned corn processing plants in the Midwest. In particular, ICI sources large volumes of corn syrup products from a facility at Dayton, Ohio. This facility is located on the rail lines of CSX Corporation (Chessie System). As mentioned above, the Atlas Point Plant of ICI is "local" to Conrail. Conrail does serve Dayton, Ohio, and historically has been afforded access to shipments originating at the supplier's plant in Dayton through reciprocal switching. Although the Chessie System rail line passes within approximately five miles of the Atlas Point Plant, that plant is not served by Chessie, either directly or through reciprocal switching. Thus, shipments destined to Atlas Point must be delivered by Conrail. Prior to 1983, this was not a problem. However, because of the various anti-competitive joint rate/route closing activities--sometimes referred to as the "traffic wars"--between Conrail and Chessie System, termination of reciprocal switching at Dayton was threatened. This would have increased the costs for sourcing material from Dayton by over $1,300 per car and would have made acquisition of this commodity from Dayton prohibitively expensive, probably resulting in a net increase in imported commodities by ICI. The latter, in addition to being more costly to ICI, would contribute to the current imbalance of the country's world trade. After much discussion with the railroads involved, ICI and its supplier were able to forestall the threatened reciprocal switching cancellation, but the subject has come up several times in the intervening years and remains a serious threat to the stability of our raw material acquisition pattern. I might add that we asked Chessie System representatives if they would be willing to seek reciprocal switching or trackage rights into the Atlas Point Plant, but they refused to do so. Their explanation was that they could not risk an attempted "invasion" of Conrail's territory for fear that Conrail would reciprocate by seeking access to closed points on the Chessie System.

Another example of the effective lack of competitive access involved ICI shipments of nitrobenzene, another bulk commodity chemical which cannot economically be moved long distances by motor carrier. ICI produces this material in Geismar, Louisiana. We had the opportunity to secure business at a destination in North Carolina served exclusively by a CSX Corporation affiliate railroad (Seaboard System). The producing plant at Geismar is local to the Illinois Central Gulf Railroad. Efforts to secure a "commodity rate" which would have made it economically feasible for us to sell a substantial quantity of nitrobenzene in the North Carolina market were unavailing. The rate would have been a "joint rate" where the Seaboard and the Illinois Central Gulf would have shared the total revenue. The competing supplier's shipping facility was located on the Seaboard. It was apparent that that railroad was unwilling to agree to a joint rate with Illinois Central Gulf which would have had the effect of diverting traffic from the nitrobenzene competitor local to their railroad, thus reducing overall CSX Corporation revenues. ICI was temporarily stymied from participating in this market for lack of a railroad commodity freight rate appropriate for this commodity chemical. The Illinois Central Gulf took action to provide an "allowance" out of its revenues accruing from the substantially higher existing rate which partially bridged the gap and enabled ICI to participate in this market, albeit at substandard profit margins. The Illinois Central Gulf's willingness to provide a reasonable rate level for this commodity chemical product is clear. If the Illinois Central Gulf, or another cooperative competing railroad, had been permitted access to the North Carolina destination, ICI believes that a reasonable price for the through transportation could have been established and ICI would then have been able to compete on a head-to-head basis with its nitrobenzene competitor based upon railroad freight rates reflecting the underlying economies of railroad transportation in lieu of the arbitrary, higher rate levels now prevailing because of the lack of intra-rail competition.

A final example of the captivity problems experienced by ICI will illustrate a peculiar effect of single railroad captivity. ICI sources a raw material from a supplier in upstate New York for use in an ICI plant in Texas. The supplier's plant is located on Conrail and is not accessible to another railroad service by either trackage rights or reciprocal switching. Conrail thus controls pricing for the movement. ICI attempted to secure a transportation price from Conrail which would permit the movement of this product via an all-rail route from New York to Texas. In spite of the fact that ICI proved to Conrail that this material was moving over the highway in tank trucks at freight rates which, if extended to tank cars, would produce revenues far in excess of the rates maintained by Conrail for competitive chemical tank car traffic for similar distances, Conrail refused to establish a rate which would even come close to meeting, let alone bettering, the direct tank truck rate. ICI would prefer to move this flammable chemical via railroad rather than over the highway, but the refusal by Conrail to establish an appropriate freight rate makes it economically infeasible to do so. ICI firmly believes that, if competitive rail access were to be provided to the New York origin, an appropriate rate level would quickly be established, based upon its knowledge of rate levels established on similar chemicals for similar distances where there is effective intra-rail competition.

The examples cited above by no means constitute an exhaustive list of the problems which ICI has experienced with rail captivity. They are only illustrative; many others could be detailed, but I do not believe that repetition is necessary to underscore the point that ICI does suffer from being a "rail captive shipper."

Many apologists for the anti-competitive actions of railroads have said either that "there are no captive shippers" or that "there are very few captive shippers" and have utilized the talents of a wide array of professional economists and others to purportedly demonstrate this lack of captivity. ICI submits that, without challenging the theoretical framework which seeks to establish the alleged lack of rail captivity, in the real world of day-to-day transport purchasing and product marketing decisions, it is definitely captive to the rail mode and to individual railroads in conducting much of its business.

ICI SUPPORTS S.447

In 1980, the Staggers Rail Act was passed and the nation's railroads and rail shippers embarked upon a journey into a brave new frontier of railroading. The mission of Staggers was of vast importance, its goals were lofty, and the words in which it was couched promised equity and balance in achieving these goals. Staggers promised a substantial reduction in the economic regulation of railroads by government. In particular, management of rail pricing was to be returned to railroad managements from the hoary halls of the Interstate Commerce Commission where it allegedly had languished over the years. The legislative history of Staggers, however, clearly recognizes the dangers inherent in untrammeled railroad monopoly power. To offset this danger, the rail transportation policy of the United States, as amended by Staggers, contains two provisions of paramount importance:

> to insure the development and continuation of a sound rail transportation system with effective competition among rail carriers...
> to maintain reasonable rates where there is an absence of effective competition...*

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* 49 U.S.C. 10101a

These provisions, it was believed in 1980, would protect the shipping public against an unbridled exercise of rail monopoly power directed against captive shippers. The promise was clear in Staggers, but that promise has not been carried out in the ensuing 5+ years since its passage. Anyone familiar with the history of the Interstate Commerce Commission's administration of the Interstate Commerce Act subsequent to Staggers is fully aware that the Commission has given primacy to the Staggers mandate to increase the financial health of the railroads--to permit them to earn "adequate" revenues. The countervailing, shipper-protective provisions of fostering intra-rail industry competition and providing, by economic regulation, reasonable rates where there is an absence of competition have been given short shrift. ICI believes that it is high time that this dismal record be rectified, so that the promises of Staggers to the shipping public and particularly to the rail-captive shipping public can be delivered.

ICI firmly believes in the ability of competition--strong, effective, real competition--to supplant economic regulation of transportation by the government. ICI has witnessed the salutary effects of opening up the airline and motor carrier industries to free competition. ICI believes that if a similar opening of the rail industry to pervasive intra-rail industry competition could be accomplished, there would be no need for government economic regulation of the rail mode. Elimination of government economic regulatory intrusion into the railroading business would be welcome not only for the positive economic benefits that would ensue, but also for the contribution towards deficit reduction that termination of the Interstate Commerce Commission would make.

ICI is not the only commentator to applaud the benefits of increasing intra-railroad industry competition. Numerous other companies and industry groups, including, but certainly not limited to, The National Industrial Transportation League, the Pro-competitive Rail Steering Committee, and the Coordinating Committee for Rail Competition (which ICI supports and on whose behalf I am also filing this statement) have publicly stated that, where there is adequate intra-rail industry competition, the Staggers Act-mandated scheme of reduced economic regulation of the railroad industry by government is working. The problem, then, for ICI and for other shippers who are to one degree or another captive to the rail mode is those instances--and there are many--where there is inadequate intra-rail industry competition.

The lack of intra-industry competition is peculiar to the rail mode among major modes of transportation. This is because of the historical anomaly of ownership of the rail rights of way by the railroad companies providing transportation over those rights of way. Ownership of the rights of way by the transportation providers raises very substantial barriers to new entrants joining the railroad transportation business. If the right of way, trackage, and other fixed facilities on a given route were owned by one company (and ICI surely does not suggest, as others have, that the rights of way ownership should be vested in the government) while use of the right of way were open to provision by a variety of companies not affiliated with the right of way-owning-company, the "captive shipper" problem would not exist, and railroad transportation could be analogous to the free market success stories of the airline and trucking industries. Of course, this is not the case and in order for the benefits of free market competition to be realized, a solution to this situation must be found.

ICI believes that S.447, the Railroad Antimonopoly Act, could go a long way towards assuring the Nation the benefits of a marketplace-oriented, competitive railroad environment. The working draft of November 12, 1985, while still requiring some refinement, if enacted could substantially improve intra-rail industry competition. It could provide a workable, reasonably certain way of opening up access to shipping and receiving locations which are presently "rail captive" in that denying a putative competitor's access to shipping or receiving facilities by a track-owning rail carrier would be prohibited. With reasonably certain prospects of success in securing access, the putative competitors presumably would not be constrained from seeking such access in order to increase their business at rates returning reasonable profits after all expenses, including a reasonable payment to the track-owning railroad, are taken into account.

S.447 is not really new law, in spite of the assertions of certain railroad interests to the contrary. In essence, it is a specific codification of a long-standing antitrust case law precedent known as the "Essential Facilities Doctrine." This doctrine was established over 70 years ago in the St. Louis Terminal Railroad Case(1), was refined and shaped by cases such as Otter Tail(2) and MCI(3), and affirmed just last year in the Aspen Skiing case(4). S.447 merely reduces the Essential Facilities Doctrine, which is a generalized body of antitrust law which has been applied to a variety of specific factual circumstances, to a particularized statute appropriate for the factual circumstances of the railroad industry. By so doing, it would reduce the uncertainties, cost, and time for filing an antitrust case against a monopolizing railroad under this doctrine. Further, by its terms, S.447 removes certain exemptions from the antitrust laws currently enjoyed by the railroad industry and provides injunctive relief under the Clayton Act. It has the important benefit of removing any uncertainty that railroads are in fact subject to the antitrust statutes where they use their monopoly power to deny competitive access.

Competitive access is the central and essential feature whose lack produces the "captive shipper" problem which afflicts ICI and many other rail shippers today. S.447 could strike a significant blow in favor of improved competitive rail access. With improved competitive access to monopolized rail facilities the monopoly power now retarding the realization of the promises of the Staggers Rail Act can be broken and those promises can begin to be realized. When this occurs, the need for governmental economic regulatory interference in shipper-rail relationships can be substantially reduced or eliminated and the need for vestigal functions of regulatory agencies such as the Interstate Commerce Commission can be greatly reduced or eliminated as well.

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(1) United States vs. Terminal R.R. Ass'n. of St. Louis, 224 U.S. 383 (1912)
(2) Otter Tail Power Co. vs. United States, 410 U.S. 366 (1973)
(3) MCI Communications Corp. vs. Am. Tel. & Tel. Co., 708 F. 2D 1081 (7th Cir. 1983), Cert. denied, 464 U.S. 891 (1983)
(4) Aspen Skiing Co. vs. Aspen Highlands Skiing Corp., No. 84-510, slip op. (U.S. Supreme Court, June 19, 1985)

ICI believes that after legislation with the thrust of S.447 has been passed, and perhaps a few test cases successfully tried under it with results favoring the free competitive access contemplated therein, the railroads will no longer resist opening up monopolized facilities to access but instead will, as the motor carriers and airlines have done, concentrate on becoming sharper competitors in a newly-freed market. By becoming, as the saying goes, "leaner and meaner" competitors, a more economical transportation service can be offered not only to captive shippers but to all shippers, and the "trickle-down" effects will be beneficial to all of the Nation's consumers. This proposed legislation, then, is not a special-interest bill--it is a consumer bill, and one whose passage should be applauded by all interests except those having the narrowest vested interests in the current monopoly situation.

ICI believes that S.447, with suitable additional amendments, will be a very worthwhile tool towards fostering increased intra-railroad industry competition and reducing the requirement for government economic regulation of commercial enterprises. ICI therefore believes this proposed legislation is worthwhile and deserving of your support and urges you to favorably consider it. Thank you for permitting ICI to express its views.

The CHAIRMAN. Mr. Mauro.

STATEMENT OF GEORGE T. MAURO

Mr. MAURO. Thank you, Mr. Chairman.

Mr. Chairman and members of the committee, my name is George Mauro, and I am pleased to appear here today on behalf of the Ad Hoc Committee on Soda Ash Transportation. I am Director of Logistics for FMC Corp. Accompanying me here today on my far right is Mr. Donald Krause, manager of purchasing and transportation for Owens-Illinois, and Mr. John K. Maser III, on my immediate right, counsel to the committee.

I have, as you indicated, submitted a prepared statement. The ad hoc committee appreciates the opportunity to present its views on the proposed Railroad Anti-Monopoly Act, as reflected in S. 447 and the subsequent staff versions of it. We support this important legislative proposal since it would enhance intramodal railroad competition and help protect captive shippers and receivers from abusive, anticompetitive, and monopolistic railroad actions.

The ad hoc committee consists of ten individual companies that are producers, shippers, and/or receivers of soda ash. But for our common interest in soda ash, we are diverse in our products, locations and mix of businesses. Together, the ten Companies employ 150,000 people.

Soda ash is the ninth most widely used chemical in the United States. It is an essential raw material in several industries, particularly in glass and chemical manufacturing, but also including the pulp and paper, water purification, cleaning compound and pharmaceutical industries. Glass manufacturers generally account for about 50 to 55 percent of total U.S. demand, and chemical producers account for another 20 percent.

The members of the committee include three of the five companies that produce soda ash in Green River, WY. These three companies also use soda ash in their chemical production facilities at various locations throughout the country. The remaining seven members of the committee are receivers of soda ash and use it in manufacturing glass, silicates, and various chemicals.

Soda ash is a bulk commodity ideally suited for rail transportation and we depend virtually exclusively on the railroad system to move soda ash to our plants all over the country.

Our member companies have receiving locations in 28 States. In addition, a substantial volume of soda ash is exported to Asia and Latin America through several gulf coast and Pacific coast ports.

In my statement I list all of the locations of our 10 companies that receive soda ash by rail. These locations are also depicted on the map on your right that is here today in the hearing room for ready reference.

The richest source of natural soda ash is trona ore. The world's largest, purest and most accessible trona reserves are located in the Green River Basin area of southwestern Wyoming, indicated on the map with the yellow star.

Green River trona has an overwhelming share of the U.S. soda ash market. The five plants there account for approximately 90 percent or some 9 million tons annually of total U.S. practical soda ash production capacity.

The railroad systems of the United States haul about 95 percent of the Green River soda ash tonnage. The Union Pacific Railroad

Co. is the only rail carrier serving Green River. It has an uncontested monopoly that extends for a minimum distance of about 150 miles to the first potential interchange with another carrier, and its average length of haul on soda ash traffic is in excess of 900 miles.

It is in this regard important to note that other major railroads also enjoy substantial long-haul participation in Green River soda ash traffic. For example, Conrail's average length of haul is in the range of 850 to 900 miles. In addition, most destination facilities of the members of the committee are served by a single terminating carrier.

In short, we have a situation where a single origin supplies 90 percent of the soda ash consumed in this country, where 95 percent of the tonnage shipped is transported by the Nation's railroads, and where a single railroad originates or participates in 90 percent of that traffic. Given this situation, it is not at all surprising that the railroads would seek to exploit their dominant position with a variety of rate and other anticompetitive practices.

For example, in comparing segments of rail routes where there is some limited competition available, in contrast to the Union Pacific's origin monopoly segment, we estimate that the revenue earned on the monopoly segment on a cents per ton mile basis are at least two to three times higher than those earned on the competitive portion of the same haul.

The dominant railroads have also taken steps to eliminate or reduce intramodal competition for the transportation of soda ash in many ways, including closing or restricting gateways and canceling joint rates and reciprocal switching agreements. In my statement I present a number of specific examples of these practices.

With the significant statutory and administrative deregulation of large segments of the railroad industry in recent years, there is today a clear gap in essential protections for captive shippers and receivers. This gap has been widely recognized by disinterested expert observers as the major failing among the many successes of railroad deregulation.

The provisions of the proposed Railroad Anti-Monopoly Act would recognize the deficiencies and uncertainties in the current situation and close that gap so that railroad competition can flourish. Free and open competition would provide the essential protections for the interests of shippers and receivers.

In essence, the proposed new section 9 of the Sherman Act would apply the essential facilities doctrine, carefully tailored to the unique nature of the railroad industry which, unlike the other major modes of transportation, controls both the transportation service and the right-of-way over which that service is provided.

In summary, the Ad Hoc Committee on Soda Act Transportation strongly supports the concepts contained in the proposed Railroad Anti-Monopoly Act. The legislation fills an important gap in the protections afforded by the current transportation and regulatory environment. It clears up any existing uncertainties regarding the application of the antitrust laws to the railroad industry and it recognizes the unique nature of today's railroad industry and provides a measured response fully consistent with established antitrust laws, principles, and remedies.

Mr. Chairman, let me just close by saying that the members of the committee are not hostile to the railroads. We deal with them every day in the normal course of business. We depend on them to provide safe and reliable transportation for our products and we need a strong, financially healthy railroad industry.

We believe that the relaxation of economic regulation has been largely beneficial and we do not wish to turn back the clock. On the contrary, we believe that enhancing intramodal competition, as this proposed legislation would do, will prove to be in the best interests of the railroads as well as their customers.

Thank you, Mr. Chairman, for the opportunity to present these views on behalf of the Ad Hoc Committee on Soda Ash Transportation. My colleagues and I would be happy to respond to any questions you or the members of the committee might have.

[The prepared statement of Mr. Mauro follows:]

STATEMENT OF GEORGE T. MAURO
On Behalf Of
THE AD HOC COMMITTEE ON SODA ASH TRANSPORTATION

Mr. Chairman and members of the Committee:

My name is George T. Mauro, and I am pleased to appear here today on behalf of the Ad Hoc Committee on Soda Ash Transportation. I am Director of Logistics for FMC Corporation, a member company of the Ad Hoc Committee, and my business address is 200 East Randolph Drive, Chicago, IL 60601. Accompanying me today are Donald R. Krause, Manager-Purchasing/Transportation, Owens-Illinois, Inc., a member company of the Ad Hoc Committee, and John K. Maser III, counsel for the Ad Hoc Committee.

The Ad Hoc Committee appreciates the opportunity to present its views concerning the important principles and concepts embodied in the proposed Railroad Antimonopoly Act, as reflected in S. 447 and the subsequent staff mark-up versions of it. The Ad Hoc Committee supports the general thrust and approach of this important legislative proposal since enactment of it would have the very salutary and needed effect of enhancing intramodal railroad competition and protecting captive shippers and receivers from abusive, anticompetitive and monopolistic railroad actions.

The Committee staff revision of S. 447 (November 12, 1985) would create a new Section 9 of the Sherman Act, under which it would be unlawful for the railroads to monopolize sole facilities under their control when those facilities are the only means of: (1) connecting with competing trackage for providing commercially practical rail service or (2) reaching a given destination. The new section would also make applicable the "substantially lessened competition" standard of Section 7 of the Clayton Act with respect to the use of sole railroad facilities. Moreover, recovery of treble damages and the cost of suit, including reasonable attorney's fees, would be permitted for violation of the new Section 9 provisions. Injunctive relief would also be permitted for threatened loss or damage by reason of a violation of the new Section 9, notwithstanding the present limitation contained in Section 16 of the Clayton Act.

The new Section 9 would make the exercise of monopoly power on the part of a railroad the unlawful act without regard as to how the monopoly came into being. If a competing carrier is used to obtain competitive transportation service over the sole facility, the owner-carrier is protected, in that Section 9 requires just and reasonable compensation to the owner-carrier for the use of its sole facilities. In this respect, the proposed language also makes it clear that in addition to allowing shippers to arrange for competitive transportation, shippers would also be able to provide the transportation service themselves.

Before I discuss the merits of the proposed legislation and the critical need for its enactment in today's railroad transportation and regulatory environment, let me turn to a discussion of the identity and interest of the members of the Ad Hoc Committee on Soda Ash Transportation vis-a-vis their reliance upon railroad transportation services in order to market, ship and receive an essential commodity, soda ash. As will be seen from this discussion, enactment of the Railroad Antimonopoly Act will add critically needed protections to captive shippers and receivers, such as the members of the Ad Hoc Committee, consistent with and in furtherance of appropriate and generally accepted antitrust, regulatory and economic principles.

The Ad Hoc Committee on Soda Ash Transportation currently consists of a group of individual companies that are producers, shippers and/or receivers of soda ash. The Ad Hoc Committee includes:

Ball Corporation
Brockway, Inc.
Desoto, Inc.
FMC Corporation
Guardian Industries Corporation
Owens-Illinois, Inc.
PPG Industries, Inc.
Stauffer Chemical Company
Texasgulf Chemicals Company
Thyssen-Bornemisza, Inc.

In the course of conducting their businesses, Ad Hoc Committee members are substantial users of rail transportation with respect to both their inbound commodities and outbound products. Ad Hoc Committee members are particularly interested in the availability of efficient and competitive rail service for the transportation of soda ash. Soda ash (chemically, sodium carbonate) is the ninth most widely used chemical in the United States. It is an essential raw material in several industries, particularly in the glass and chemical industries, but also including the pulp and paper, water purification, cleaning compound, and pharmaceutical industries.

The members of the Ad Hoc Committee include three of the five companies which produce soda ash at facilities at or near Green River, Wyoming. These three members also ship soda ash from Green River to various other facilities throughout the country. The remaining members of the Ad Hoc Committee are receivers of soda ash which utilize that commodity in the manufacture of glass, silicates, and various chemicals. Glass manufacturers generally account for approximately 50-55% of total U.S. soda ash demand while chemical manufacturers account for approximately 20% of demand.

The members of the Ad Hoc Committee alone receive soda ash at the following locations:

Ball Corporation

Carteret, NJ
Dolton, IL
Asheville, NC
Okmulgee, OK
Washington, PA
El Monte, CA

Desoto, Inc.

Joliet, IL
Orange, CA
Columbus, GA

Brockway, Inc.

Montgomery, AL
Freehold, NJ
Zanesville, OH
Ada, OK
Oakland, CA
Danville, VA
Brockway, PA
Muskogee, OK
Lapel, IN
Pomona, CA

FMC Corporation

Houston, TX
Clearing, IL
Carteret, NJ
Philadelphia, PA
Baltimore, MD
City of Industry, CA
Newark, CA
Atlanta, GA
Lawrence, KS
Chicago, IL
Detroit, MI
Rosedale, CA
Buffalo, NY
Syracuse, NY
Ringoes, NJ
Jeffersonville, IN
Midland, MI
Nashville, TN
Jersey City, NJ
Burlington, IA
Lake Charles, LA
Cleveland, OH
Columbus, OH
Wixom, MI
Cincinnati, OH
Pittsburgh, PA
N. Haven, CT
Moapa, NV
Charlotte, NC
Oklahoma City, OK
Pt. Arthur, TX

Guardian Industries

Ash, MI
Sunmaid, CA
Corsicana, TX

Owens-Illinois, Inc.

Chicago Heights, IL
Streator, IL
Toano, VA
Big Island, VA
Charlotte, MI
Clarion, PA
Columbus, OH
Ellers, NC
Hapeville, GA
Shreveport, LA

Owens-Illinois, Inc. (con't)

South Volney, NY
Wisconsin Dam, WI
Huntington, WV
Vineland, NJ
City of Industry, CA
Toledo, OH
Fir, OR
Los Angeles, CA
Oakland, CA
Tracy, CA
Waco, TX
Lakeland, FL
Olivers Mills, PA
Mt. Pleasant, PA
Parkersburg, WV

PPG Industries, Inc.

Mt. Zion, IL
Crystal City, MO
Mt. Holly Springs, PA
Stony Point, PA
South Lexington, NC
West Shelby, NC
Lake Charles, LA

Stauffer Chemical Corporation

Baton Rouge, LA
Buffalo, NY
Carnegie, PA
Chattanooga, TN
Chicago Heights, IL
Chicago, IL
Cleveland, OH
Detroit, MI
Fairburn, GA
Flemington (Ringoes), NJ
Henderson, NV
Houston, TX
Jefferson, IN
Joliet, IL
Memphis, TN
Nashville, TN
Pittsburg, CA
Southgate, CA
Tacoma, WA
Wasco, CA

Texasgulf Chemicals Company

Atlanta, GA
Bradenton, FL
Buffalo, NY
Carnegie, PA
Cincinnati, OH
Chicago, IL
Cleveland, OH
Jeffersonville, IN
Philadelphia, PA

Thyssen-Bornemisza, Inc.

Laurens, SC
Henderson, NC
Ruston, LA
Seattle, WA
Lincoln, IL
Port Allegheny, PA
Madera, CA

Attachment A to this statement depicts the above facilities graphically on a map of the United States. While the number of facilities depicted there is large, showing facilities in the states of Alabama, California, Connecticut, Florida, Georgia, Illinois, Indiana, Iowa, Kansas, Louisiana, Maryland, Michigan, Missouri, Nevada, New Jersey, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, Tennessee, Texas, Virginia, Washington, West Virginia and Wisconsin, it is significant to note that many additional facilities of other companies (numbering in the hundreds) also utilize soda ash and receive it by rail. Soda ash is, indeed, an essential commodity in our country's economy and its use is widespread throughout the country.

In addition, a substantial volume of U.S.-produced soda ash is exported and sold to foreign glass manufacturers and other users, particularly in Asia and South America. The U.S. producers have formed the American Natural Soda Ash Company (ANSAC), an Export Trading Company Act corporation, to coordinate their international marketing efforts. Through this medium, some 15% of U.S. domestic production is exported. These export shipments are made through a number of Gulf- and

Pacific-coast ports, in particular Longview, Washington, Portland, Oregon, Long Beach, California, and Port Arthur, Texas.

The richest source of natural soda ash is trona ore. The purest, world's largest and most accessible trona reserves are located in the Green River Basin area of Wyoming. Green River trona has an overwhelming share of the U.S. soda ash supply market, with Green River producers consistently accounting for approximately 90% of total U.S. practical soda ash production capacity: Green River capacity is approximately 9 million tons of soda ash annually, while total United States production capacity is approximately 10.3 million tons.*

The railroads' share of total Green River soda ash shipments approximates 95%. The Union Pacific Railroad Company is the sole originating rail carrier serving the Green River producing area and its average length of haul is in excess of 900 miles. The addition of the Missouri Pacific and Western Pacific Railroads to the Union Pacific system in 1982 extended the dominance of this combined railroad system even further with respect to participation in Green River soda ash traffic.*

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* Soda ash also occurs (in less pure form) as a natural constituent in the mineral deposits of certain springs and lake brines. The production of natural soda ash through the direct carbonation of natural brine occurs in the United States at facilities located at Searles Lake, California. However, Searles Lake only accounts for 10-12% of practical U.S. soda ash capacity. Soda ash can also be manufactured synthetically. Historically, synthetic soda ash plants produced the vast majority of soda ash consumed in the United States. In 1939, 17 synthetic soda ash plants were operating in the United States. However, due to various environmental, energy and economic factors, as of today, there are no synthetic plants operating in the United States. The last remaining synthetic plant (the Solvay plant located near Syracuse, New York) ceased operation, effective January 1, 1986. The only Canadian synthetic soda ash plant (the Amherstburg plant located in Ontario) primarily serves Canada and has a capacity which is insufficient to supply even the soda ash requirements of Canadian industries. Indeed, a substantial amount of Green River soda ash is exported into Canada for the use of Canadian industries.

In response to the absolute control over originating Green River soda ash traffic exercised by the Union Pacific system, several truck/rail transfer oprerations have been developed within the past few years. These operations, in which the soda ash is moved by truck from Green River to a transloading facility on another railroad, provide a mechanism for other rail systems to gain access to this desirable traffic. However, the inherent inefficiency of multiple loading/unloading operations;

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* Union Pacific Corporation is the parent company of the Union Pacific System railroads, which includes Union Pacific Railroad, Missouri Pacific Railroad, and the former Western Pacific Railroad. Union Pacific Corporation also controls the Rocky Mountain Energy Company, which now possesses the mineral rights in approximately one-half of the total Green River soda ash reserves and which are located on land originally given to the Union Pacific Railroad under the Pacific Railroad Acts. Act of July 1, 1862, 12 Stat. 489-92; Act of July 2, 1864, 13 Stat. 356. According to Union Pacific Corporation's 1985 "Second Quarter Report," Union Pacific System's second quarter earnings of $81.9 million were up 14% from 1984 earnings. Operating income was ahead of 1984 and the operating ratio improved over 1984. Similarly, according to this report, Rocky Mountain Energy Company's earnings of $10.3 million were equal to last year's "as improved soda ash prices offset a decline in coal income...." Clearly, soda ash and the transportation of it by the Union Pacific System railroads makes a significant contribution to the undeniable good health and profitability of the Union Pacific corporate family.

the additional time involved in driving several hundred miles from Green River to rail sidings in Bonneville, Wyoming or Ogden, or Salt Lake City, Utah; and the capacity limitations of trucks, truck-loading facilities at the Green River plants, and storage and railcar loading facilities at the transloading points are, individually and conjunctively, major impediments to the growth of this multimodal system.*

In addition to the dominance of the Union Pacific system in soda ash traffic, it is important to note that other major rail carriers also enjoy substantial long-haul participation in Green River soda ash traffic as connecting carriers with the Union Pacific system. For example, Conrail's average length of haul is 850 to 900 miles. In addition, most destination and receiving facilities of the members of the Ad Hoc Hoc Committee are served by a single terminating carrier.

Moreover, the Green River soda ash producers and receivers have made multi-million dollar capital investments in rail-related facilities. The producers provide approximately 50%

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* Truck/rail transfer operations only account for approximately 4-8% of Green River soda ash shipments. Direct motor carrier service from Green River to destination points is also very limited (amounting to approximately 2% of shipments) and does not provide effective competition for the movement of soda ash from Green River, Wyoming due to the long-haul, bulk-loading, high volume nature of the soda ash movements. In the vast majority of cases, the costs of trucking soda ash from Green River to destination points are prohibitively high due, among other things, to the long distances involved (generally ranging from 900 to 2,000 miles) and to the unavailability of regular backhaul movements and adequate equipment. Effective water carrier competition is also not available, since Green River, Wyoming is not located on a navigable waterway.

of the covered hopper railroad cars used to transport Green River soda ash through their ownership or control of a fleet in excess of 4,000 cars. At current prices, the value of this investment alone exceeds 160 million dollars. In addition, they have built and maintained miles of in-plant trackage and storage facilities. Soda ash receivers have also made substantial investments in rail bulk unloading, storage, trackage and conveyor systems related to their receipt of soda ash.*

In short, with respect to Green River soda ash, there exists a situation where the Green River origin alone supplies almost 90% of the soda ash consumed in this country, where over 95% of such Green River soda ash traffic is transported by the nation's railroads, and where a single railroad system (the Union Pacific System) originates and/or participates in the transportation of over 90% of the Green River soda ash traffic. Moreover, railroad shipments of Green River soda ash can be expected to increase due to the recent closing of the last domestic synthetic plant, the Solvay plant, in January of this year, as previously discussed. That plant had accounted for approximately 7% of the market.

Given the above situation, it is not surprising that the railroads would seek to exploit their dominant position with respect to the transportation of Green River soda ash through the extraction of excessive and unreasonable rates, as well as the imposition of anticompetitive practices. In fact, abuse has occurred and continues to occur. Among other things, the dominant railroads have taken steps to eliminate or reduce intramodal competition for the transportation of soda ash in many ways, including the closing of gateways and the cancelling of joint rates and reciprocal switching agreements.

For example, in 1981 the Union Pacific cancelled joint rates on soda ash when routed via the Ann Arbor Railway System as an overhead carrier, following the Ann Arbor's decision not to join in a 7% increase in joint rates which was authorized by the Interstate Commerce Commission. This "flag-out" by the Ann Arbor resulted in a substantial increase in the amount of traffic routed via the Ann Arbor routes and a corresponding decrease in alternative, higher rated routes of the Union Pacific and other connecting carriers. However, even though the Union Pacific continued to participate in all rail originated Green River soda ash traffic, including traffic routed on the Ann Arbor, and even though Union Pacific's division or share of the joint rate on soda ash traffic routed via the Ann Arbor continued to be very profitable to it, the Union Pacific nonetheless cancelled all joint rates on this traffic when routed via the Ann Arbor and Ann Arbor's participation in soda ash traffic ceased completely, thereby preventing shippers and receivers from having this competitive alternative and lower rates available to them.

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* It is noted in this respect that glassmaking facilities, which utilize the majority of soda ash production as an essential ingredient in the glassmaking process, operate on a 24-hour, seven day per week basis due to production and technical requirements. Thus, a continuous supply of soda ash is absolutely necessary for continued operation. No other raw materials can replace soda ash as an essential material in glassmaking.

Another example is the action of the Union Pacific in 1983 of "closing" (i.e., providing that tariff rates do not apply via or in connection with traffic interchanged with another railroad) its Grand Island, Nebraska gateway with the Burlington Northern Railroad, thus protecting the Union Pacific from competition over that gateway and ensuring the Union Pacific of the long-haul over its Council Bluffs, Iowa or Kansas City, Missouri gateways. In 1982 the Union Pacific also closed its Ogden, Utah gateway, thereby restricting receivers to the Union Pacific's Los Angeles interchange and effectively eliminating the alternative route over the Southern Pacific via Ogden with respect to certain California destinations.

Similarly, other railroads, both intermediate and destination carriers participating in Green River soda ash traffic, have closed gateways, restricted routing or cancelled reciprocal switching in order to eliminate competition and assure themselves of the long haul. In 1983, for example, the Illinois Central Gulf Railroad closed its Memphis, Tennessee gateway which resulted in the unavailability of intermediate carriers and competitive alternatives to certain destinations. In 1983 the Southern Railway (now Norfolk Southern) closed its Birmingham, Alabama gateway with the Burlington Northern system, thereby forcing all soda ash through Norfolk Southern's Memphis gateway with respect to destinations in the South. To interchange Green River soda ash traffic with Southern at any other points would have subjected the receiver to higher rates and drastically increased transportation costs. Gateway and routing restrictions have likewise been imposed by the Seaboard System Railroad on Green River soda ash shipments to destinations in Florida which are served solely by that carrier (such traffic must be routed via Cairo, Metropolis, or East St. Louis, Illinois or Memphis, Tennessee gateways), and by Conrail with respect to certain eastern destinations served by that carrier (such traffic must be interchanged to Conrail at Chicago, Illinois and/or St. Louis, Missouri).

As final examples of the anticompetitive actions which have been taken place involving Green River soda ash traffic, I note the Union Pacific's action in 1982 of increasing its rate to its Denver, Colorado interchange point by approximately 60%, thereby eliminating the use of lower proportional rates via connecting carriers on soda ash shipments to destinations in the Southwest. Similarly, the rates to the St. Louis gateway were increased by 32% in 1979 and the rates to the Chicago, Chattanooga and Nashville gateways were subjected to a series of increases starting in 1983, all with the effect of reducing competitive alternatives. Other rate and tariff actions by the Union Pacific and other carriers of a similar nature and with a similar effect of reducing competitive alternatives could also be cited.

Beyond this, railroad rate levels have risen over the years to excessive and supra-competitive levels.* In response to this situation, certain members of the Ad Hoc Committee were complainants before the Interstate Commerce Commission in a formal complaint case initiated pursuant to Section 229 of the Staggers Rail Act of 1980, wherein the reasonableness of the rail rates on soda ash originating at Green River, Wyoming moving to more than 150 destinations located throughout the United States were challenged.**

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* Railroad transportation rates for the movement of soda ash generally average over 75% of the cost of soda ash and in many instances exceed 90% of the cost. Although in terms of weight soda ash represents only 12-18% of the total raw materials (batch) used in glassmaking, the delivered cost of soda ash represents approximately 55-60% of total batch costs.

** The rates subject to complaint were those in existence on October 1, 1980, the effective date of the Staggers Act. Complainants' evidence demonstrated that the challenged rates produced before-tax rates of return as high as 119.2% and resulted in revenue to variable cost ratios as high as 319%. Those rates, which were established collectively by the railroads through rate bureau proceedings, were, in short, well above reasonable, competitively set levels. The challenged rates, according to complainants' evidence, exceeded a maximum reasonable level by as much as 100%, with an average excess of at least 45%. The complainants had also participated in many, earlier ex parte proceedings before the Commission opposing the imposition of general rate increases on the soda ash traffic. Notwithstanding this shipper opposition, all general rate increases authorized by the Commission had been applied in full by the railroads to the complaint rates since 1974 with one exception. The one exception was the flag-out by the Ann Arbor Railroad of the 7% increase authorized by the Commission in Ex Parte No. 357 in 1978. As I discussed earlier, the Ann Arbor's participation in the soda ash traffic ceased when the Union Pacific cancelled all joint rates on soda ash when routed via the Ann Arbor.

In a decision served June 10, 1985, the Commission never even reached the issue of whether or not the challenged rates were unreasonable, finding instead, that it did not have jurisdiction to adjudicate this issue since it found that the railroads did not possess market dominance, as it interpreted that term. In so doing, it reversed an earlier determination by its administrative law judge who found the presence of market dominance. The Commission's decision is the subject of a pending petition for judicial review before the U.S. Court of Appeals for the District of Columbia Circuit. The important point for our purposes, however, is that the Commission's "hands-off" approach -- the absence of vigorous and appropriate regulatory oversight and control concerning dominant railroads' pricing and service practices -- emphasizes the importance of the antitrust approach which is here before the Committee today.*

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* In this respect, I would note that current rail rates via the Union Pacific, as originating carrier, are still at excessive and supra-competitive levels. The success of the limited truck/rail transfer operations I described earlier is the best recent evidence I can cite. Despite the inherent inefficiencies of these services when compared to all-rail service, they are apparently being operated at a profit. One of the founding partners of the Bonneville operation recently estimated that the rates his company offers, in conjunction with the Burlington Northern Railroad, are $500 to $1500 per carload below those charged by the Union Pacific. It is interesting to note that the newspaper report containing this information begins with the sentence: "Will giant Union Pacific Railroad (UP) put a fledgling trucking firm out of business for carving a small slice out of UP's monopoly on hauling soda ash out of southwestern Wyoming?" "Western Business," January 1986 - Vol. 3, No. 6.

The absence of effective and balanced regulatory oversight on the part of the Interstate Commerce Commission serves to highlight the necessity for consideration and enactment of the concepts and provisions contained in the proposed Railroad Antimonopoly Act. There are, however, more fundamental and compelling reasons to amend the Sherman Act in the careful, specifically tailored, fashion proposed. With the significant statutory and administrative deregulation of large segments of the railroad industry in recent years, reflected in such laws as the Railroad Revitalization and Regulatory Reform Act of 1976 and the Staggers Rail Act of 1980, especially as interpreted and implemented by the Interstate Commerce Commission, there has come into being a clear gap in essential protections for captive shippers and receivers of rail transportation service and much uncertainty concerning the application of the antitrust laws to the railroad industry.

Clearly, a major goal of both the so-called 4-R Act and the Staggers Rail Act was, and is, the encouragement and promotion of increased rail competition, and the protection of captive shippers and receivers. See, e.g., 49 U.S.C. §§10101a(1), (4) and (6). However, precisely the opposite has in fact been allowed to occur in many instances.* Thus, on the one hand,

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* Many examples of inadequate and ineffective regulatory oversight have been presented to this Committee at earlier hearings concerning this proposed legislation. While I will not burden the record with repetition in this respect, the Committee's attention is directed to such decisions of the Interstate Commerce Commission as: I.C.C. Docket No.

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significant amounts of railroad traffic have been deregulated or withdrawn from effective oversight on the part of the Interstate Commerce Commission, while, at the same time, the railroads are largely unrestrained in significant respects from abusive and anticompetitive practices under the existing antitrust laws, as interpreted by the Courts over the years.*

Reference can here be made, for example, to the so-called Keogh doctrine which was enunciated by the Supreme Court of the United States in 1922 in Keogh v. Chicago & North Western Railway Company, 260 U.S. 156 (1922), and which is well known

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39021, Midtec Paper Corporation v. Chicago and North Western Transportation Company (served July 17, 1985), appeal pending, No. 85-1476, Midtec Paper Company, et al. v. U.S.A. and I.C.C., (D.C. Circuit) [reciprocal switching and use of terminal facilities]; I.C.C. Finance Docket No. 29883, Universal Forest Products Inc. v. Seaboard Coastline Railroad Company (served June 23, 1983) [reciprocal switching]; I.C.C. Docket No. 38676, Changes in Routing Provisions - Conrail - July, 1981 (served March 22, 1982), reversed, Chesapeake and Ohio Ry. Co. v. U.S., 704 F.2d 373 (7th Cir. 1983) [joint rate cancellations]; I.C.C. Docket No. 39176 (Sub-No. 1), Pittsburgh and Lake Erie Railroad Company v. Consolidated Rail Corporation (served April 9, 1985), appeal pending, No. 85-1312, Pittsburgh and Lake Erie Railroad Company v. U.S.A. and I.C.C. (D.C. Circuit) [joint rate and route cancellations]; Joint Line Cancellation - Soda Ash - Union Pacific R. Co., 365 I.C.C. 951 (1982) [joint rate cancellations].

* It is also to be recognized that the statutory standards utilized by the Interstate Commerce Commission under such provisions as 49 U.S.C. §§11103 (reciprocal switching and use of terminal facilities), 10705 (joint rates and through routes), 11344 (mergers) and 10101a(3) (railroad revenue adequacy) are different from antitrust law standards used by courts.

to this Committee. While this doctrine is subject to substantial challenge in the light of recent changes to the regulatory structure in recent years, as discussed above, the fact remains that it has been applied in recent decisions to prohibit recovery by injured shippers and receivers. See, e.g., In the Matter of Wheat Rail Freight Rate Antitrust Litigation, 759 F.2d 1305 (7th Cir. 1985), appeal pend'g, sub nom. Little Crow Milling Co., Inc. v. B&O R.R., No. 85-112, ___ U.S. ___ (1985).

In addition, Section 16 of the Clayton Act specifically prohibits injunctive relief by private parties, such as shippers and receivers, where railroad common carrier operations are subject to the jurisdiction of the Interstate Commerce Commission. Here again, the provisions of the proposed Railroad Antimonopoly Act would recognize the deficiencies and uncertainties of the current situation and close the gap so that railroad competition can truly begin to flourish and essential protections can be accorded to injured private parties.

In essence, the proposed new Section 9 to the Sherman Act would permit application of the "essential facilities" doctrine,*

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* The U.S. Court of Appeals for the Seventh Circuit set forth the four elements necessary to establish liability under the essential facilities doctrine in MCI Communications v. American Tel. & Tel. Co., 708 F.2d 1081, 1132-1133, (7th Cir. 1983), cert. denied, 464 U.S. 891 (1983), as follows: (1) control of the essential facility by a monopolist; (2) a competitor's inability practically or reasonably to duplicate the essential facility; (3)

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tailored in a careful and specific fashion in recognition of the special nature of the railroad industry. Indeed, the rail mode is unique among the major modes of transportation in that private owners control both the transportation service and the right of way over which that service is provided. Public ownership and maintenance of the rights of way and associated facilities used by motor carriers, airlines, ocean carriers, and barge operators insures free and open competition in every market. By definition, no shipper or receiver can be "captive" to a single trucking company. It is this competitive freedom -- the potential for unfettered entry or exit -- that makes it feasible for Congress to consider, as it will this year, the full and complete elimination of economic regulation of motor carriage. Allowing competing railroads access to each other's "essential facilities" on just and reasonable terms is a necessary step to allow the competitive marketplace to function.

The proposed legislation would recognize the "bottleneck" nature of many railroad facilities -- essential facilities which

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the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility. See also Hecht v. Pro-Football, Inc., 570 F.2d 982, 992-93 (D.C. Cir. 1977), cert. denied, 436 U.S. 956 (1978); Otter Tail Power Co. v. United States, 410 U.S. 366 (1973); United States v. Terminal Railroad Association, 224 U.S. at 405, 409 (1911); City of Mishawaka v. American Electric Power Co., 465 F. Supp. 1320, 1336 (N.D. Ind. 1979), aff'd in relevant part, 616 F.2d 976 (7th Cir. 1980), cert. denied, 449 U.S. 1096 (1981).

are in place even though a given railroad may not have taken affirmative steps to acquire its monopoly over an essential facility. It is a fact of life that in a number of situations a railroad's ownership of the underlying right-of-way, trackage, switches, equipment, etc., gives that railroad monopoly power, that is, it can control prices or exclude competitors with respect to the transportation service over the bottleneck or essential facility. The proposed legislation would provide for a remedy in those situations where a remedy is necessary to prevent abuse with respect to captive shippers and receivers.

It bears repeating that the proposed Railroad Antimonopoly Act provisions, including the remedies provided for therein, are fully consistent with existing antitrust principles and remedies.* It is important to emphasize in this respect, however, that, even though the proposed legislation is consistent with established antitrust principles, it is still necessary to amend the Sherman Act as proposed in order to give railroad shippers and receivers a clear cause of action in dealing with an individual railroad monopoly situation. Moreover, the proposed protections are narrowly drawn, giving due consideration to the distinctive nature of railroad physical plant and operations in this country.*

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* Antitrust courts have employed various remedies with respect to the use of a defendant's facility, including compensation remedies, when access is mandated under the "essential facilities" doctrine. *See*, *e.g.*, *United States v. Terminal Railroad Association*, *supra*, 224 U.S. at 411 ["just and reasonable terms and regulations"]. *Otter Tail Power Co. v. United States*, *supra*, 410 U.S. at 375 ["compensatory" rates]; *MCI Communications v. American Tel. & Tel. Co.*, *supra*, 708 F.2d at 1133-1141 ["reasonable" and "nondiscriminatory" terms]; *Byars v. Bluff City News Co.*, 609 F.2d 843, 864 (6th Cir. 1979) [history of dealing between parties can provide basis for a "fair" price]; and, *United States v. Standard Oil Co.*, 362 F. Supp. 1331, 1342 (N.D. Cal. 1972), *aff'd*, 412 U.S. 924 (1973) ["shared cost" basis.]

Indeed, the need for corrective action takes on increasing importance when one considers the severe contraction in the number of Class I railroads and the concomitant reduction in intramodal railroad competition in recent years. In the past 20 years the number of major Class I railroads has declined from approximately 100 such carriers to less than 20 Class I railroads today. More importantly, a limited number of huge, powerful railroad systems has evolved. This would include the Burlington Northern, CSX Corporation, Norfolk Southern, Conrail, and the Union Pacific systems. In addition, the Santa Fe-Southern Pacific merger is pending before the Interstate Commerce Commission at this time. There is also an effort being made, of course, to combine Norfolk Southern and Conrail, and the Senate has already passed the enabling legislation which would permit this combination. These six, huge existing railroad systems together control in excess of 85% of all railroad traffic in this country today. Individual origin and destination facilities, of course, in many cases are captive to a single railroad or railroad system with respect to essential transportation services. Soda ash traffic originating in Green River, Wyoming, as discussed above, is a prime example of this type of captivity.

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* Use of a competing carrier, for example, would require conformance to generally accepted safety, scheduling, and related aspects of the operation and management of trains, without impeding the monopolist's ability to serve its customers, consistent with established "essential facilities" doctrine. Moreover, an owner-carrier would receive just and reasonable compensation for the use of its sole facilities by a competing carrier. Charges imposed by the owner-carrier on other railroads for similar use privileges, such as trackage rights, could well serve as the basis for the just compensation standard of the new Section 9. Trackage rights are used widely in the railroad industry today and often for long distances involving hundreds of miles of trackage. See, e.g., Union Pacific - Control - Missouri Pacific, Western Pacific, 366 I.C.C. 458 (1982). It should be noted in this respect, however, that the I.C.C. is not authorized to impose trackage rights generally, where not related to a particular rail merger proceeding, or where terminal facilities or reciprocal switching are not involved.

In summary, the Ad Hoc Committee on Soda Ash Transportation strongly supports the concepts and principles contained in the proposed Railroad Antimonopoly Act. The proposed legislation fills an important gap in the protections afforded by the current antitrust laws in today's transportation and regulatory environment and it clears up existing uncertainties regarding the application of the antitrust laws to the railroad industry. The proposal recognizes the unique nature of the railroad industry in our country today and provides a measured and tailored response, fully consistent with established antitrust law principles and remedies.

I will close by emphasizing that the members of the Ad Hoc Committee are not hostile to the railroads; they recognize the mutual interest in having a healthy and viable railroad system. Moreover, as shippers and receivers these companies have supported the railroad deregulation movement of recent years, as embodied in the Staggers Rail Act provisions, for example. Much good has resulted from the substantial loosening of the regulatory controls of the I.C.C. At the same time, however, meaningful protection of captive shippers and receivers, as well as the enhancement of intramodal railroad competition, is absolutely necessary and in the overall public interest. The concepts and principles contained in the proposed Railroad Antimonopoly Act will help ensure that these protections are available if needed.

Thank you, Mr. Chairman, for the opportunity to present these views on behalf of the Ad Hoc Committee on Soda Ash Transportation.

FMC Corporation

Executive Offices
200 East Randolph Drive
Chicago, Illinois 60601
312 861 6000

FMC

March 24, 1986

The Honorable Strom Thurmond
Chairman, Committee on the Judiciary
United States Senate
218 Russell Senate Office Building
Washington, D.C. 20510

Re: S. 447, The Railroad Antimonopoly Act

Dear Chairman Thurmond:

This will respond to the questions posed in your letter of March 7, 1986 concerning my testimony on behalf of the Ad Hoc Committee on Soda Ash Transportation at the March 4, 1986 hearing of your Committee. The Ad Hoc Committee on Soda Ash Transportation strongly supports S. 447 since it would enhance intramodal railroad competition and help protect captive shippers and receivers from abusive and anticompetitive railroad actions.

The two questions presented and our responses are set forth below:

Question

> The Interstate Commerce Commission has developed distinct procedures for dealing with "captive shipper" problems such as those which you have described. What are the reasons for your belief that it is necessary to involve the courts in this process, rather than to depend upon the I.C.C. procedures, or even, to seek amendment to any procedures which are deemed ineffective?

Response

The procedures developed by the Interstate Commerce Commission do not provide adequate protections for captive shippers and receivers for several important reasons. First, the procedures recently adopted by the I.C.C. in Ex Parte No. 445 (Sub-No. 1), Intramodal Rail Competition, do not, by their express terms, reach the critically important subject of railroad trackage rights as a means of providing competitive access to captive shippers and receivers. Indeed, Chairman Gradison of the I.C.C. acknowledged in her testimony at the March 4, 1986 hearing before the Committee that the I.C.C. does not even have jurisdiction over trackage rights of the type which are addressed in S. 447. Thus, enactment of S. 447 is necessary in order to provide needed protections to captive shippers and receivers, consistent with established principles of antitrust law, such as the "essential facilities" doctrine.

Secondly, the I.C.C.'s Ex Parte No. 445 (Sub-No. 1) rules, which have not yet been applied in an actual case, are essentially procedural in nature. The president of the Association of American Railroads, one of the proponents of the Ex Parte No. 445 (Sub-No. 1) rules, in response to concerns raised by several members of The National Industrial

Transportation League who were involved in the negotiations that produced those rules, wrote that "...the agreement in no way relates to whether railroads will, or will not, cancel rates. The agreement relates, rather, to the procedures and standards to be employed by the parties and the ICC in disputes over the cancellation or establishment of joint rates and reciprocal switching arrangements."

Thirdly, the Administration is now proposing to "sunset" the I.C.C. and transfer its residual regulatory responsibilities to several Executive branch agencies. While the legislation to accomplish this transfer has yet to be offered for Congressional consideration, it seems reasonable to assume that these successor agencies will be free to adopt, modify, or reject in toto any presently existing rules or procedures of the I.C.C. In this regard, we are not encouraged by the views Administrator Riley of the Federal Railroad Administration expressed on the problem of intramodal railroad competition in his testimony before the Committee on March 4, 1986.

Finally, even if we assume that the I.C.C. will continue to exist for the long term, contrary to current efforts to sunset the agency or to provide zero budgeting for it, it is not at all clear that either the current majority of the I.C.C., or successor majorities, would implement the Ex Parte No. 445 (Sub-No. 1) rules in an aggressively procompetitive manner. The I.C.C.'s pattern of behavior over the past five and one-half years, since enactment of the Staggers Rail Act of 1980, is cause for serious alarm and concern in this respect.

The I.C.C.'s hostility to vigorous and enhanced intramodal competition, as well as its failure to protect captive shippers and receivers from abusive and anticompetitive rates and practices, are reflected in many recent cases. For example, in I.C.C. Docket No. 38891, Central States Enterprises, Inc. v. Seaboard Coast Line Railroad Company, in a decision of the I.C.C. (by Commissioners Andre, Gradison, Sterrett, with then-Chairman Taylor dissenting) served May 15, 1984, the I.C.C. reversed an earlier decision of its Review Board which had found that the performance of reciprocal switching was practicable, in the public interest and necessary to provide competitive rail service. One of the key reasons given by the I.C.C. for denying the requested reciprocal switching was the so-called "revenue inadequacy" (as defined by the I.C.C.) of the railroad with the local monopoly. Thus, in essence, the I.C.C. was concerned with protecting "competitors" and not with protecting "competition," unlike the focus of antitrust relief of the type S. 447 would afford for captive shippers and receivers.

Similarly, in I.C.C. Docket No. 39021, Midtec Paper Corporation, et al. v. Chicago & North Western Transportation Company, in a decision of the I.C.C. (by Commissioners Andre, Sterrett, Strenio and then-Vice Chairman Gradison, with then-Chairman Taylor and Commissioners Simmons and Lamboley dissenting) served July 17, 1985, the I.C.C. again reversed earlier decisions of its Review Board and Administrative Law Judge which had ordered reciprocal switching, even though the requested reciprocal switching was entirely feasible and practical and even though it was needed by the involved shipper to afford it competitive rail rates, alternatives routings, access to additional sources of supply, as well as for other competitive reasons. Not only did the decision of the then and current majority of the Commission deny the competitive access requested, it overruled the decisions of its Review Board and Administrative Law Judge and discarded its own precedents to impose a wholly new set of standards to be applied in reciprocal switching and terminal facilities cases. The best critique we can offer of the impact of this decision is to quote from the dissent of then-Chairman Taylor as follows:

> "Finally, in denying the relief sought by complainants, a majority of the Commission has established a new standard to govern requests for reciprocal switch-

> ing and joint use of terminal facilities, which requires a showing of market dominance and rate unreasonableness as a prerequisite to relief. In my view, this new standard is illogical, contrary to the statute, and totally inconsistent with Congressional intent.
>
> "The Staggers Act represents a balancing of competing interests. On the one hand, the railroads were provided substantially more rate freedom than existed under the prior law. On the other hand, Congress sought to counter-balance the railroads' new freedoms by providing shippers additional protection through the procompetitive access provisions of the Act. To superimpose the very essence of the railroads' rate freedom (namely, the market dominance and rate unreasonableness standards) on top of the provisions designed to protect shippers by providing a counterbalance to such freedom (namely, the procompetitive access provisions) renders these shipper protective provisions totally meaningless and undermines the carefully crafted balancing of interests Congress sought to achieve in the Staggers Act. In fact, the new standard adopted by the majority in this proceeding no[t] only fails to embrace the concepts designed to promote more competition in the rail industry, but it also heralds [a]n openly permissive attitude toward anticompetitive conduct."

A final example out of the many that could be cited is the I.C.C.'s handling of so-called "DT&I" traffic protective conditions with respect to railroad merger proceedings. For many years the I.C.C. had frequently imposed conditions on mergers to guard against potential anticompetitive effects. However, in its decision in Ex Parte No. 282 (Sub-No. 5), Rulemaking Concerning Traffic Protective Conditions in Railroad Consolidation Proceedings served March 19, 1982, the I.C.C. declared, among other things, that these "DT&I" conditions would be removed from all existing mergers, across-the-board. Thereafter, on judicial review of this I.C.C. decision, the U.S. Court of Appeals for the Sixth Circuit, in Detroit, Toledo & Ironton R. Co. v. U.S. and I.C.C., 725 F.2d 47 (6th Cir. 1984), reversed and remanded the I.C.C. decision, stating that the I.C.C.'s decision to remove DT&I conditions from all previously approved mergers "is fatally flawed because of its total failure to consider, as required by Congress, the effect of its ruling on regional rail competition." (725 F.2d at 50) The court went on to observe the following:

> "In its zeal to carry out one part of its congressional mandate -- encouraging greater rate flexibility and improved competitiveness with other modes of transportation -- the Commission has apparently lost sight of another part of its mandate -- considering the effect of its proposals on competition within the railroad industry itself." (Id. at 57)

In short, given the track record of the I.C.C. and the absence of effective and balanced regulatory oversight, given the significant statutory and administrative deregulation of large segments of the rail industry in recent years and given the current deficiencies and uncertainties involving the application of the antitrust laws with respect to the railroad industry, the members of the Ad Hoc Committee on Soda Ash Transportation strongly support enactment of the Railroad Antimonopoly Act as the only effective remedy to the problem of encouraging rail-to-rail competition.

Question

> The legislation provides that just and reasonable compensation be paid to the rail owner for competitive access over its lines. This determination is to be made by the court -- which would adjudicate any disputes. This sounds quite like rate regulation, which you have said you oppose, in favor of free competition amongst railroads. How would you propose to remedy this situation?

Response

In the view of the Ad Hoc Committee on Soda Ash Transportation the proposed Railroad Antimonopoly Act can and should properly be considered as a rail access bill, not a rail rate regulation bill. If a violation is found under the provisions of the new law and access is ordered by the court in an appropriate case, it would be our expectation that the court would order the involved railroads to attempt to reach an accommodation as to compensation and related issues, so as to permit operation over the sole railroad facility. This is the approach normally taken by the court and the parties in other essential facilities cases. See, e.g., United States v. Standard Oil Co., 362 F. Supp. 1331 (N.D. Cal. 1972), aff'd., 412 U.S. 924 (1973). Thus, the court would not normally become involved in setting the level of the compensation to be paid to the rail owner for competitive access over its lines. The court would only be available to determine such issues if the parties are unable to resolve such issues voluntarily.

In this connection, we would point out that trackage rights are widely used in the railroad industry today. Under such arrangements, the involved railroads agree to the terms and conditions, including compensation issues, operational issues, and safety issues. Indeed, in her recent testimony before the Committee on March 4, 1986, Chairman Gradison of the I.C.C. noted that there are many outstanding trackage rights agreements in which the railroad parties have been able to reach agreement as to such competitive access issues. Moreover, such agreements in many cases involve distances of many hundreds of miles.

Therefore, we would not expect that it would be necessary for the antitrust court to become involved in determining the just and reasonable compensation to be paid in most instances. If this should become necessary, however, the courts are clearly capable of dealing with this type of issue in the context of railroad competitive access, as they have in other essential facility cases involving other industries, such as the telecommunications industry. See, e.g., MCI Communications v.

American Tel. & Tel. Co., 708 F.2d 1081 (7th Cir. 1983), cert. den., 464 U.S. 891 (1983). In addition, it is important to note that the courts would not become involved with "rate regulation" as that term is used in the question presented. Under the provisions of S. 447, the issue concerns the level of the charge for access as between the railroads involved, not the rate level charged the shipper or the receiver by the railroad for providing the transportation service itself in terms of transporting the goods or commodities from origin to destination. Both railroads would then be free to compete for the traffic at issue, charging whatever rates they choose. Thus, "rate regulation" is not an issue under the proposed Railroad Antimonopoly Act.

* * *

On behalf of the Ad Hoc Committee on Soda Ash Transportation, I trust that the above answers have been responsive to the inquiries of the Committee on the Judiciary concerning this important matter. We appreciate the opportunity to present our views to the Committee in support of the proposed legislation. We stand ready to provide further responses should you have any additional questions. Please do not hesitate to contact us.

Respectfully submitted,

George T. Mauro

On Behalf of the Ad Hoc
Committee on Soda Ash
Transportation

:jmw

cc: Members, Committee on the Judiciary
United States Senate

Senator DECONCINI. Thank you. The chairman had to leave for other commitments. He is President pro tempore and he asked me to continue the hearings and he has a couple of questions which I will read to you and if you could answer them for the record.

Let me ask you about the rules recently adopted by the ICC which were the result of agreements among railroads and shippers. How could those changes help to solve the problems of shippers that are being addressed by this bill?

Mr. Long, would you like to answer that?

Mr. LONG. Yes, I would be glad to respond to that. I was part of the committee on behalf of the National Industrial Transportation League that negotiated with a corresponding group in the Association of American Railroads, and so I do have some background in that.

Those rules are viewed as procedural rules. Bill Dempsey, of the AAR, has stated that publicly and I think that is pretty well acknowledged. They are not substantive rules.

Second, those rules do not deal with trackage rights. Trackage rights were not a negotiable item in the process of those negotiations.

Furthermore, the rules have yet to be put into the setting of an actual case or controversy where their efficacy can be demonstrated. Certainly, the Interstate Commerce Commission prior to this time has not demonstrated any inclination at all to provide increased competition as a means of mitigating the problems that captive shippers face.

Quite frankly, we feel more direct, more substantive relief in the form of S. 447 would be a more appropriate means. We would favor competition as the regulator of the railroads, rather than the Government as the regulator of the railroads, and we think this bill will go a long way toward that end.

Senator DECONCINI. If I understand it, these rules which are part of the process do not deal with trackage rights.

Mr. LONG. That is correct.

Senator DECONCINI. That is a fundamental problem here.

Mr. LONG. They deal only with joint rates and route cancellations and reciprocal switching.

Senator DECONCINI. I am advised that the antitrust rules proposed by this bill go beyond the existing Sherman Act standards and are tailor made to this particular industry. What arguments can be made for such special treatment legislation? This is a question by Chairman Thurmond.

Mr. LONG. I would ask counsel to join in this, but from a layman's point of view my understanding is that what is essentially proposed here is a specific codification of case law known as the Essential Facilities Doctrine, which ironically enough arose originally in a railroad setting back in the early 1900's in the *St. Louis Terminal Railroad* case.

I believe that what is proposed would simply expedite the procedures in the Federal court system for securing relief under the antitrust laws by specifically tailoring the codified doctrine to the railroad setting. I do not believe it would produce remedies that are not a part of the case law now. I would defer to counsel for an expansion on that.

Senator DECONCINI. Mr. Donovan.

STATEMENT OF PAUL M. DONOVAN

Mr. DONOVAN. Thank you, Senator. One must view the railroad industry in historic context when examining this legislation. The Sherman Act, the first antitrust law, was passed in 1890. The railroads were already regulated by the Interstate Commerce Commission at that point, hence not only the antitrust statutes but all antitrust case law were developed over a period of time where the railroads were completely exempt because of the regulatory situation.

Most importantly, railroad consolidations were approved by the Interstate Commerce Commission without regard largely to the criteria of section 7 of the Clayton Act which otherwise would have applied, hence to say that this bill treats railroads separately and distinctly from every other industry is true; however, the antitrust laws have always treated the railroads separately. They have been exempted under section 16 of the Clayton Act——

Senator DECONCINI. There would be no fundamental change of Government policy as it relates to the railroads by the fact that you pass some legislation specifically treating railroads.

Mr. DONOVAN. That is largely true. The argument that was made this morning by the chairman or at least alluded to by the chairman, Chairman Thurmond, was that perhaps we should just make the railroads completely subject to the antitrust laws, without more. I suggest if that is true, then section 7 of the Clayton Act would effectively become retroactively applicable and we probably would break up every railroad system in the country, which I think is an overreaction.

STATEMENT OF JOHN K. MASER III

Mr. MASER. Senator, if I may add briefly, I would concur in what Mr. Donovan has said. I would also point out that in one sense you could view the railroads as having had the benefit of special antitrust legislation all of these years, for example, in section 16 of the Clayton Act. What this bill would do is help to rectify that situation, particularly in the light of the substantial deregulation which has occurred.

And might I also take the opportunity, while I have the floor, to point out in response to one thing that Chairman Gradison of the Commission mentioned concerning the standards for reasonableness and so forth that the ICC has in place, according to the Chairman. Those apply in a coal rate context—in fact, they are called coal rate guidelines—there are no applicable standards, comparable standards that the Commission has in place for noncoal traffic such as soda ash with which we are concerned here, and in fact the Commission has not addressed that specifically at this point.

Therefore, it is not fair to say simply that those standards are in place now and that everything will roll forward smoothly without problems.

Thank you.

Senator DECONCINI. Mr. Mauro, in response to your testimony, and your fine explanation with your map, why couldn't your shipment east leave the Union Pacific tracks at Cheyenne and your company benefit from the competitive rate at that point?

Mr. MAURO. Senator DeConcini, I think we might indeed welcome that, since the closest available interchange going east is Council Bluffs or Fremont in the Omaha area.

The problem is that there are no competitive combination or joint rates published today available to us over a Cheyenne interchange between the Union Pacific and the Burlington-Northern system. So in effect, even though the physical connection exists, in effect that gateway, if you will—and I am hesitating over these words because much has been made of the history of gateway closings and the response has been no gateways have been closed. Well, certainly that is physically true, but when rate actions are taken in such a way as to discriminate against traffic that is moved over a historically viable and physically viable route, that has the effect of closing the gateway. That is the situation in Cheyenne.

Mr. Krause, who is on the receiving end, may want to comment.

Mr. KRAUSE. The only thing I want to say in addition is that the Union Pacific not only will not allow a connection at Cheyenne with the Burlington-Northern, it in fact closed its gateway one step further east at Grand Island, NE, to the Burlington-Northern, leaving Council Bluffs.

Senator DECONCINI. So you have no other alternative?

Mr. KRAUSE. No other alternative whatsoever.

Senator DECONCINI. Mr. Donovan, let me just ask you a general question. You have helped the committee and testified before and have been very helpful to the committee. Were you here when the new Chairperson was making her testimony?

Mr. DONOVAN. Yes, I was.

Senator DECONCINI. Do you have any comments that you would like to make regarding that previous testimony?

Mr. DONOVAN. As tempting as that may be, on a very high plain without regard—and I think Mr. Riley made some comments that the problem, if any, exists as an ad hominen problem, a problem with people—I do not think that is the case at all.

The Interstate Commerce Commission is a regulatory body, and I am reminded of a situation comparing the Interstate Commerce Commission and its regulatory functions over railroads, with industry generally regulated by competition. If I am in an industry generally and I produce a product for 100 and my market price is $180 and some chap comes to me and says I have found a way to cut your costs in half so that instead of costing you $100 it costs you $50, your profit goes from $80 to $130, I take the fellow home and introduce him to my daughter, he is a hero.

On the other hand, if the same thing happens in the railroad industry and you have this 180 percentage of variable cost cap as a regulatory benchmark, now the railroads' profitability goes from $80, which is the difference between $100 and $80, which is lawful, and $50 and $90, which then becomes lawful. You have just cost yourself $40. That is a built-in disincentive to efficiency, and if inefficiency drives the market we are going to have high costs and inefficiency. If competition drives the market, we are going to have low cost and efficiency. That is good for the railroads and it is good for the shippers. I do not think the ICC can respond.

Senator DECONCINI. So maybe the criticism of the ICC is too much on my part. Your point is well taken.

Gentlemen, thank you. The record will remain open for 2 weeks if anyone wants to supplement their testimony.

The committee will stand in recess, subject to the call of the Chair.

Thank you very much.

[Whereupon, at 11:52 a m., the committee was recessed, to reconvene subject to the call of the Chair.]

APPENDIX

BALTIMORE
GAS AND
ELECTRIC

CHARLES CENTER · P. O. BOX 1475 · BALTIMORE, MARYLAND 21203

CHRIS H. POINDEXTER
VICE PRESIDENT
ENGINEERING AND CONSTRUCTION

1985 SEP 20 AM 9:30

September 18, 1985

The Honorable Strom Thurmond
Chairman, Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Senator Thurmond:

Subject: The Railroad Antimonopoly Act
S. 447

Thank you for inviting me to offer my views on this important legislation. As you may know, I presented a statement to the House Judiciary's Subcommittee on Monopolies and Commercial Law on June 27, 1985, when they were considering H. R. 1140, the companion bill to S. 447.

I have attached a copy of my comments in support of the legislation then before the House Subcommittee. I would very much appreciate it if you would enter them into the record of your Committee's deliberations.

Very truly yours,

CH Poindexter

CHP:MDP:crs

Attachment

STATEMENT OF

CHRIS H. POINDEXTER
VICE PRESIDENT-ENGINEERING AND CONSTRUCTION
BALTIMORE GAS AND ELECTRIC COMPANY

BEFORE THE
SUBCOMMITTEE ON MONOPOLIES & COMMERCIAL LAW
OF THE JUDICIARY COMMITTEE
U.S. HOUSE OF REPRESENTATIVES
JUNE 27, 1985

Good Morning. My name is Chris H. Poindexter, and I am the Vice President-Engineering & Construction of the Baltimore Gas and Electric Company. We appreciate very much the opportunity to give you our thoughts for your consideration in your deliberations on the Railroad Antimonopoly Act of 1985.

Our Company provides 2.3 million people with electricity in a 2300-square mile area of Central Maryland. I believe that we are a fairly typical East Coast utility company in terms of our changing fuel usage. Ten years ago, we were predominantly an oil-burning company. In the last decade, we have added new nuclear and coal-burning units to our system as well as converted older units back to coal with new air pollution control devices. Today, we generate less than 5% of our electricity with oil. Our use of coal is currently 2.5 million tons per year and, with the completion of our new Brandon Shores Unit 2, we will burn 4 million tons of coal per year. I believe that coal will be the dominant fuel source for additions to the nation's electric system for the foreseeable future. In Baltimore Gas and Electric Company's case, we have already announced that the next unit for service in the mid-90's will be a coal-burning plant.

Competition in all aspects of our fuel procurement is vital in achieving our goal of maintaining the prices for our electricity as low as possible. The transportation of coal is one aspect of that process where we believe there is insufficient competition. In the absence of competition, regulation is used in many parts of our economy to control prices. No one understands that any better than the electric utility industry. However, in the case of coal transportation, there is little competition, and regulation has been essentially removed. I am sure that there are a number of witnesses who will testify and cover all of the technical aspects of ICC regulations and proceedings.

In summary, let me say that we do not believe that under current law and regulations, there is sufficient protection for the so-called captive shipper.

We have taken a number of steps in an attempt to lower our costs of fuel transportation. At our Brandon Shores plant, we have invested almost $40 million in a marine coal delivery system which has, to a limited extent, enhanced our *competitive position by providing access to other carriers. For the past two years, we have advocated that the Maryland State Legislature pass enabling legislation to permit a coal pipeline to be considered. The conceptual feasibility studies envisioned a pipeline from the coal fields of West Virginia and Western Maryland into the port of Baltimore. The railroads, primarily CSX, mounted a strong lobby and have been able to block the passage of this legislation. They enjoy their monopolistic position and do not want any competition.*

We are also supporting the recently introduced Coal Pipeline Act of 1985. As I'm sure you know, this has been blocked for many years in Congress. However, we feel strongly about it and will continue the battle.

I have studied all the testimony from the hearing before the Senate Committee on the Judiciary considering their companion bill to HR 1140 (S 447). Witnesses testifying against the proposed legislation indicated that there is no problem with competition in coal transportation. Curiously, however, all of the people who pay the freight bills for the transportation of coal think that there is a very severe problem. As an example, BG&E operates one power plant which receives all its coal by single rail carrier. In 1983, the rates applicable to shipments of coal from mines not served by the destination carrier were cancelled. After two years of difficult negotiations, we have reestablished joint line service to this plant under a contract. This contract expires in several years, and we expect substantial difficulty renegotiating joint line service.
We believe this problem is aggravated by the consolidation that is currently going on among the nation's rail systems and by the diversification of the railroads into the other modes of transportation available for the shipment of bulk commodities.

The Railroad Antimonopoly Act of 1985 will help in our efforts to maintain price stability for our electric customers. In our opinion, it will operate to accomplish this without the introduction of additional detailed regulation. That appears to be consistent with the direction in which our nation is moving. In your deliberations, we urge you to consider that as captive shippers we are concerned about the current situation where regulation has been essentially removed without the presence of real competition. The Railroad Antimonopoly Act of 1985 will be a help to remedy this situation. We urge the Subcommittee to vote favorably on HR 1140.

BEFORE THE
COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

STATEMENT OF JAMES R. SNYDER
CHAIRMAN, LEGISLATIVE COMMITTEE
RAILWAY LABOR EXECUTIVES' ASSOCIATION

ON S. 447

SEPTEMBER 24, 1985

My name is James R. Snyder. I appear before you today as Chairman of the Legislative Committee of the Railway Labor Executives' Association. I am also National Legislative Director of the United Transportation Union.

The Railway Labor Executives' Association is an unincorporated association with which are affiliated the chief executive officers of all of the standard national and international railway labor unions in the United States. The organizations whose chief executive officers are members of the RLEA are listed below:

American Railway & Airway Supervisors Association, Division of BRAC
American Train Dispatchers Association
Brotherhood of Locomotive Engineers
Brotherhood of Railroad Signalmen
Brotherhood Railway Carmen of the United States and Canada
Brotherhood of Railway, Airline and Steamship Clerks, Freight Handlers, Express and Station Employes
Hotel & Restaurant Employes and Bartenders International Union
International Association of Machinists and Aerospace Workers
International Brotherhood of Boilermakers and Blacksmiths
International Brotherhood of Electrical Workers
International Brotherhood of Firemen & Oilers
International Longshoremen's Association
National Marine Engineers' Beneficial Association
Railroad Yardmasters of America
Sheet Metal Workers' International Association
Seafarers International Union of North America
Transport Workers Union of America
United Transportation Union

I present to you this statement on behalf of the railroad employees in the United States represented by the members of the RLEA in opposition to the enactment of S. 447.

Railroad employment in this country has dropped sharply over the past 40 years. From a high of 1.6 million employees after World War II to less than 550,000 in 1980; and from 514,000 on July 1, 1981 to 388,000 on January 1, 1983--a drop of 25% in just

18 months. For the moment at least employment seems to have stabilized at about 400,000.

One can readily understand therefore, our concern regarding proposed legislation which would have an adverse effect upon railroad jobs or job opportunities.

The objective of S. 447, which is to provide equal access to competitive transportation services, is appealing on its face but the manner in which the bill would achieve that objective is highly objectionable to the people who work on the railroads.

A reading of S. 447 indicates to us that if it were to be enacted employment opportunities in the railroad industry would be seriously diminished and many of our members with many years of service in this industry would become unemployed.

Section 3 of the bill would make it unlawful for a carrier which owns the sole railroad facility to a point to "deny . . . any shipper . . . the use . . . of [that] facility which is the sole facility over which such shipper can move bulk commodities by rail to connect with the track of a competing rail carrier or to reach the destination of shipment."

By its plain language, therefore, this provision would authorize any shipper to lease a locomotive and cars, hire a few employees off the street at any wage they might accept, and proceed to transport its shipments from or to the line of the nearest competitor of the railroad whose line it is using. Such a result would have devastating effects upon the jobs of the rail employees of this country. Shippers would become cut rate railroads taking the work away from the employees of the railroads now performing that work. At best it would serve only as a mechanism to cut the wages for those few railroad employees who could obtain work with the shipper-short line railroads while depriving those employees of their collective bargaining and representation rights.

In recent years, the railroad industry has been deluged by a vast number of short line railroads created by small entrepreneurs from lines of railroad which the owning railroads desired to sell but which they could not abandon because they were profitable or because of public need for them. Obviously, the creation of short lines manned by their owner, relatives and friends of their owners, and by former railroad employees desperately seeking work are able to serve their customers at cut rates because their wages are cut rate. Many bona fide railroad jobs have been lost because of the creation of these short lines and S. 447 would intensify this problem.

The exception in S. 447 to a shipper's authorization to perform the rail transportation itself is if the carrier owning the tracks permits another rail carrier upon "reasonable rental of track" to use the owning carrier's tracks to serve that shipper.

The term "rail carrier" is defined in the bill as "a person or persons providing for compensation railroad transportation in or affecting commerce." It would seem that under such a definition the rail carrier using the owning carrier's line would have to be an established, recognized railroad but that is not the case.

Section 10901 of the Interstate Commerce Act governing the extension or construction of lines of railroad and the acquisition or operation of extended or additional lines by "a rail carrier providing transportation subject to the jurisdiction of the Interstate Commerce Commission" has been interpreted by the Commission to apply to companies not subject to I.C.C. jurisdiction; that exist only on paper and were created by entrepreneurs to purchase and operate lines of railroad with non-union employees at substandard pay. The I.C.C. theory is that these companies will become "carriers providing transportation" and will become "subject to the jurisdiction of the I.C.C." when the I.C.C. approves their applications. This interpretation by the Commission has been upheld by federal Courts of Appeals.

Applying the same interpretation to the definition of "rail carrier" in S. 447 could result literally in dozens of non-union paper companies being created by rail competitors or by private individuals to operate over the owning railroads' lines at cut rates. Needless to say, such a result would be extremely detrimental to the employees of the railroads involved, their rail employers and ultimately the public.

S. 447 would have severe and extensive anti-railroad employee and anti-organized labor effects and RLEA vigorously opposes its enactment.

Thank you.

FMC Corporation

Executive Office
200 East Randolph Drive
Chicago, Illinois 60601
312 861 6000

1985 OCT -3 AM 9 30

FMC

October 1, 1985

Senator Strom Thurmond
Chairman, Committee on the Judiciary
United States Senate
Washington, DC 20510

Re: Railroad Antimonopoly Act of 1985 S. 447

Dear Mr. Chairman:

FMC Corporation supports rail deregulation. As a major user of rail services, we applaud the progress made by U.S. railroads since 1980 in upgrading their operations and improving their financial performance. But if rail deregulation is to be successful, individual railroads cannot be permitted to abuse their inherent monopoly control of access to the rail system by foreclosing access to economically efficient rail to rail competition.

A fundamental premise of deregulation is that the forces of free market competition will best protect the interests of shippers and consumers. Railroads are in a unique position to exclude competition by virtue of their individual control over rights-of-way and associated facilities. The combination of this monopoly control, increasing concentration in the railroad industry, and virtually unlimited pricing freedom, have allowed and encouraged the railroads to frustrate rail to rail competition.

The ICC has recently adopted a set of rules that may result in some increased access to more than one carrier. But this is essentially an abuse of monopoly power problem that should respond to normal market forces subject to normal antitrust standards. Today such practices are arguably exempt from antitrust enforcement. By affirming that railroads cannot use their facilities to monopolize access to the railroad system, S. 447 would increase rail to rail competition and reduce the need for regulatory control.

Various versions of S. 447 are being discussed. FMC urges passage of a Bill that would apply to all products, would include both injunctive and damage remedies, and would clearly remove any "Keogh" or other exemption or immunity from the antitrust laws relative to use of facilities to monopolize rail movement. We respectfully request that this letter be made part of the Committee record.

Sincerely,

Leo H. Everitt

Leo H. Everitt, Jr.
Vice President Manufacturing

PHOSROCK
Phosphate Rock Export Association

September 30, 1985

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
224 Dirksen Senate Office Building
Washington, D.C. 20510

Re: S.447: The Railroad Antimonopoly
Act of 1985

Dear Senator Thurmond:

I am writing on behalf of the Phosphate Rock Export Association ("Phosrock") to express its strong support for S.447, the Railroad Antimonopoly Act of 1985. The Florida phosphate industry is essentially totally dependent upon a monopolist railroad, Seaboard Coastline Railroad, for the movement of phosphate products from the mines and processing facilities in Central Florida to the Port of Tampa, approximately 40 miles to the West. As there is no other alternative but to use the railroad services of Seaboard Coastline, this monopolist railroad has been able to exact ever increasing rail charges for the services it provides. Indeed, current rail charges to port account for over 25% of the F.O.B. mine value of the phosphate rock sold by Phosrock in the export market and create the serious disability for Phosrock as it competes in international markets against overseas rivals who are not encumbered in this way and, indeed, who often have the strong support of their respective governments.

I am attaching to this letter a brief description of Phosrock's operations and the remarkable disparity between Florida phosphate rock export prices and inland transportation rates. During the last ten years, phosphate prices have decreased by 38 index points while, at the same time, rail freight and handling charges have increased 140 index points.

Phosrock strongly supports the principles of S.447 and urges its enactment.

Sincerely yours,

James J. Galvin
Chairman of the Board and
Chief Executive Officer

1311 N. West Shore Blvd. — Suite 301, Tampa, Florida 33607, U.S.A. ☐ Telephone (813) 879-7310 · Telex 52-633 · Cable PHOSROCK
Mailing Address: Post Office Box 23626, Tampa, Florida 33623-3626, U.S.A.

STATEMENT OF
PPG INDUSTRIES, INC.

PPG Industries, Inc. ("PPG") hereby submits this written statement to the Senate Judiciary Committee for consideration during deliberations on S.447, The Railroad Antimonopoly Act of 1985. PPG wishes to express its appreciation to the Senate Judiciary Committee for this opportunity to present its views on this most important matter involving competitive access to railroad transportation facilities.

PPG is a multi-division, multi-facility corporation with manufacturing plants and other interests throughout much of the free world. In 1984, PPG's net sales were $4.2 billion dollars, and the company employed approximately 38,000 persons worldwide, approximately 27,000 of whom are in the United States.

PPG is a substantial user of rail transportation. More than 35 percent of PPG's United States tonnage moves by rail. Approximately 66 percent of PPG's rail tonnage moves over joint routes involving two or more railroads. The company owns over 3,000 rail cars which are operated throughout the United States. These cars have a replacement value of more than $200 million.

PPG has predominant interests in the northeastern portion of the United States where 29 of its 39 domestic plants are located. Thirteen of the plants located in the northeast are served by Conrail. Of these, 12 are captive to Consolidated Rail Corporation with no other railroad serving these plants. PPG's Natrium, West Virginia chemical plant is served exclusively by the Chessie System and in 1984 originated approximately 7,300 carloads of which chlorine and caustic soda represent 76 percent.

PPG operates a major chemical manufacturing complex at Lake Charles, LA, and another chemical plant in Chaison, TX, near Beaumont, TX. In 1984, the Lake Charles plant originated approximately 14,000 carloads of rail traffic and the Chaison facility originated 900 carloads of rail traffic. Both plants are jointly served by the Kansas City Southern Railroad and the Southern Pacific Railroad. The Lake Charles plant is also served by the Union Pacific-Missouri Pacific Railroads via reciprocal switching arrangements. PPG ships a substantial volume of batch raw materials by rail to and from our glass and fiberglass plants, the largest of which is located in Wichita Falls, TX on the Missouri-Kansas-Texas Railroad. We are therefore vitally interested in the preservation of competitive rail service via efficient joint routes and rates.

During the five years since the passage of the Staggers Rail Act of 1980, PPG has grown increasingly concerned about the failure of the Interstate Commerce Commission to curtail anticompetitive conduct on the part of the large Class I railroads of the United States. Primarily, through the cancellation of joint rates and routes with connecting railroads and the termination or monopolistic pricing of reciprocal switching services, these railroads have eliminated alternative routes by which shippers were able to obtain competitive service options and rate reductions. Through cancellation of joint rates and terminations of reciprocal switching, railroads have been able to divert traffic from connections, and reroute that traffic via their high revenue, long haul routes. In the process, connecting rail carriers have been foreclosed from competing for portions of the cancelling railroad's long haul movements.

The Interstate Commerce Commission has permitted virtually all of these cancellations and reciprocal switching terminations to become effective without any investigation or analysis as to the competitive characteristics or efficiency of the routes cancelled or the long haul routes left open. Finally, last year in response to Senate pressure created by the introduction of Joint Resolution 331, the ICC initiated two Ex Parte proceedings[1] which resulted in the adoption of so-called competitive access regulations which are intended to deal with cancellations of joint rates and routes. (The ICC refused to consider separate provisions dealing with reciprocal switching).

PPG participated actively in these proceedings before the Interstate Commerce Commission to develop meaningful regulations which would have sufficient specificity and enforceability to preserve efficient competitive routing alternatives for rail dependent shippers. Unfortunately, our review of the proposal adopted by the Interstate Commerce Commission during its open conference on September 11, 1985 indicates that the Commission will promulgate general, and in some cases, ambiguous regulations which may not provide meaningful relief and will require protracted litigation before the Commission. We are particularly concerned with the Commission's disposition of such cases since it has repeatedly shown that it fails to understand the importance of the Congressional mandate for increased intramodal competition as a marketplace control over excessive rail rates.

Critics of S.447 contend that the ICC's adoption of competitive access regulations have solved the competitive access problem, but this is not the case. In the Staggers Rail Act of 1980, Congress explicitly articulated its policy of maximum reliance on competitive market conditions to govern the reasonableness of rail rates and the quality of rail service. However, given its recent decision on reciprocal switching[2] and its refusal to adopt effective competitive access regulations, it is now clear that the Interstate Commerce Commission lacks either the ability or inclination to vigorously implement this policy with respect to the railroad industry. PPG has therefore concluded that further steps are necessary to ensure that the Commission's inadequate competition policies are supplemented with alternative measures that will enable shippers to utilize the well-established principles of the antitrust laws to deal with the problems of anticompetitive foreclosure of rates, routes and reciprocal switching by large railroads.

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[1] Ex Parte No. 456, The Staggers Rail Act of 1980-Conference of Interested Parties and Ex Parte No. 445 (Sub-No. 1), Intramodal Rail Competition.

[2] Midtec Paper Corporation, et al. v. Chicago and North-western Transportation Company (Use of Terminal Facilities and Reciprocal Switching Agreement), Docket 39021, August 7, 1985, appeal pending Midtec Paper Corporation v. I.C.C., 85-1476 (C.A.D.C.) (ICC refused to grant terminal trackage rights or reciprocal switching to enable shipper to obtain access to competitive rail service.)

The availability of the antitrust remedies in S.447 will have a salutary and cautionary affect on the actions of a railroad which attempts to eliminate competition by rate and route cancellations or terminations of reciprocal switching. Passage of this legislation would restore the economic and legal balance between railroads and rail dependent shippers who presently have no effective remedy against anticompetitive foreclosures undertaken by a cancelling railroad. The proposal currently under consideration by this Committee would redress that imbalance. It will provide shippers and competitively foreclosed railroads with an alternative means of opposing unjustified cancellations or reestablishing efficient competitive joint rate and route relationships.

Furthermore, PPG believes that the availability of this type of antitrust remedy would provide significant incentives to the railroads to conduct detailed examinations of their cancellations for possible anticompetitive consequences before publishing those cancellations. Moreover, there would also be strong incentives for railroads to engage in meaningful pre-cancellation negotiations with connections and with affected shippers to arrive at equitable and efficient rate and route arrangements if all parties were aware that arbitrary and abusive practices would be subject to the full penalties of the antitrust laws.[3] Thus, S.447 will complement the ICC's competitive access regulations and aid in their effective implementation by private parties directly involved in these matters.

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[3] Pre-cancellation negotiations will be required under the ICC's competitive access regulations, but the ICC refused to provide incentives for the railroads to conduct meaningful negotiations. S.447 would provide those incentives to insure equal bargaining positions.

PPG has carefully examined the provisions and rationale of S.447. With slight modifications, PPG believes that this legislation will provide an essential supplement to the regulatory measures adopted by the Interstate Commerce Commission. PPG recommends that the definition of the term "rail carrier" not be restricted to common carrier rail service. Over half of all rail traffic today moves in contract service under 49 U.S.C. §10713 or is exempt from regulation under 49 U.S.C. §10505. As "rail carrier" is presently defined in S.447, it can be argued that the cause of action and remedies provided by the bill pertain only to shipments or service provided by an "owner rail carrier" as a common carrier. This limitation, in effect, could permit an "owner rail carrier" to "contract" its way out of any liability under this bill. The definition of "rail carrier" should encompass all types of service provided by the railroad industry.

PPG also urges the Committee to amend the definition of the term "connect" to specify that such connections be commercially practical, operationally safe and efficient, and suitable for the interchange of traffic between the "owner rail carrier" and the connecting railroad. These changes would reflect the fact that many points of connection between railroads are not adequately designed for prompt or efficient interchange operations. An owner rail carrier should not be able to avoid liability under this provision by agreeing to interchange with a connecting line over a track connection which will not provide a viable, commercially competitive route.

Moreover, PPG notes that this bill provides a cause of action to "any person" injured in this business or property or threatened by such injury. PPG understands that this language would provide not only shippers but connecting railroads and other parties with standing to seek relief under the act. The legislative history of this bill should contain an explicit statement of that intent. The very fact that a competing connecting rail carrier is granted a cause of action under the antitrust laws will have a significant affect on the ability of those carriers to negotiate satisfactory revenue divisions with the owning rail carrier and thereby avoid the necessity of shippers having to file lawsuits under this provision. Attached as Appendix I to this statement are specific draft proposals incorporating PPG's modifications to Section 9(c)(1) and (7) for the Committee's consideration.

Finally, this legislation should address the issue of primary jurisdiction as it pertains to the Interstate Commerce Commission's diminishing regulatory authority over railroad rates and practices. The legislation will not provide injured parties with effective relief if railroad defendants can obtain referral of factual issues to the ICC which has repeatedly refused to promote inter-railroad competition. The courts are fully competent to deal with competitive foreclosure of essential facilities and need not rely on whatever residual expertise remains at the ICC.

With these minor modifications, PPG believes that this legislation will provide a strong and important contribution to the creation and preservation of effective rail-to-rail competition in the United States while at the same time reinforcing the procompetitive national rail transportation policy articulated by Congress in the Staggers Rail Act of 1980.

In sum, PPG strongly believes that the railroad industry should be subject to the antitrust laws in the same manner as any other competitor in our national economy. The Staggers Rail Act of 1980, as implemented by the Interstate Commerce Commission, has virtually eliminated Interstate Commerce Commission jurisdiction over railroad rates and practices. The collective establishment of railroad rates under antitrust immunity provided by the Reed Bullwinkle Act has been substantially curtailed. Railroads, however, are by statute not subject to injunctive relief under the antitrust laws, and are protected from private treble damage suits by the antiquated and outdated Keogh Doctrine. This legislation would eliminate those "safe havens" for railroads from the antitrust laws with respect to competitive access issues. If railroads seek to conduct their business and price their services in a deregulated, competitive marketplace, they can no longer lay claim to the special status of a regulated industry operating under preferential exemptions from the antitrust laws.

APPENDIX I

TO STATEMENT OF PPG INDUSTRIES, INC.

PROPOSED REVISIONS TO S.447

Section 9(c)(1) 'rail carrier' means a carrier providing, for compensation, railroad transportation in or affecting commerce.

Section 9(c)(7) 'connect' includes connections from the point of origin, point of destination or point of interconnection with another carrier which permit the commercially practical and safe interchange of rail shipments.

PROCOMPETITIVE RAIL
STEERING COMMITTEE

Suite 410. 1090 Vermont Avenue. NW
Washington. DC 20005
(202) 842-3870

October 17, 1985

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
SD-224 Dirksen Senate Office Building
Washington, D.C. 20510

Re: S. 447, The Railroad Antimonopoly Act of 1985

Dear Mr. Chairman:

The purpose of this letter is to provide to the Senate Committee on the Judiciary, and to you as its Chairman, the comments of the Procompetitive Rail Steering Committee (Procompetitive Committee) on S. 447, the Railroad Antimonopoly Act of 1985.

Identification Of The Procompetitive Committee

The members of our Committee are industrial companies which are tied to the railroads by production facilities designed for rail service and by distribution systems geared to long-distance, high-volume shipments which are generally not adaptable to transportation by truck or intermodal service. Efforts to change this dependence on rail service could not be accomplished without massive capital infusions and unacceptably high increases in operating costs. In addition the products shipped by some members of the Procompetitive Committee are fungible, bulk and low-value goods with rail transportation costs representing a significant percentage of their delivered value.

The membership of the Procompetitive Committee comprises the following:

Allied Corporation
American Iron and Steel Institute
Amoco Chemicals Company
Cargill, Incorporated
Celanese Chemicals Company, Inc.
CF Industries, Inc.
Chrysler Corporation
Colt Industries, Inc.
Ethyl Corporation
Ford Motor Company
FMC Corporation
ICI Americas, Inc.
International Paper Company
Libbey-Owens Ford Company
Manville Service Corporation
Monsanto Company
Nalco Chemical Company
Occidental Chemical Corporation
Olin Corporation
Owens-Illinois, Inc.
PPG Industries, Inc.
Reichhold Chemicals Inc.
Tennessee Eastman Company,
Division of Eastman Kodak
Union Carbide Corporation
Uniroyal, Inc.
Wyandot Dolomite, Inc.

The Necessity For Vigorous Intramodal Railroad Competition

Because of their substantial dependence upon rail service the members of the Procompetitive Committee have been deeply concerned about two developments which have been taking place. The first is the continuing reduction, due to mergers and consolidations, in the number of railroads serving the public and the enormous potential for abuse of railroad monopoly power by such carriers to the severe injury of the shipping public. The second is the actual and growing number of instances where the railroads have indulged in anticompetitive action to prevent or obstruct the ability of other railroads to serve the shipping public by participating in available routes of movement under truly competitive rates.

The Procompetitive Committee's Consideration Of S.447

In its efforts to obtain a solution which would ensure vigorous intramodal railroad competition the Procompetitive Committee has become aware of S. 447, the Railroad Antimonopoly Act of 1985 and the similar legislative proposal before the House Judiciary Committee. Our Committee is also aware of possible modifications of S. 447 which have been brought forth in the course of the analysis, presentations, and the hearings on the bill. The Procompetitive Committee is gratified to note that S. 447 and related, modified versions address the concerns of the Procompetitive Committee on some of the key aspects of railroad competitive access. The members of the Committee are actively engaged in studying and evaluating this proposed legislation and, upon completion of this work, will further communicate its views to you and to your Committee.

Procompetitive Committee Approach To Issue Of Intramodal Rail Competition

The members of our Committee have devoted much time and effort to finding a solution which will preserve, strengthen and promote vigorous intramodal railroad competition. The Committee has collaborated in studies and has prepared a working draft of proposed legislation to help resolve the problems. We enclose as Attachment No. 1 a Report to the Procompetitive Rail Steering Committee by Dr. Curtis Grimm, Assistant Professor, Transportation, Business and Public Policy, College of Business Management, University of Maryland. This report is entitled "Preserving and Promoting Rail Competition". Attachment No. 2 is the Legislative Proposal of the Procompetitive Rail Steering Committee directed to achieving intramodal rail competition. Attachment No. 3 is a Section-by-Section summary of that legislative proposal.

We submit these attachments in the hope that the approach there taken to the problems of railroad competitive access will be of interest to you and your colleagues on the Senate Judiciary Committee.

The Procompetitive Committee appreciates the concern of the Senate Judiciary Committee evidenced by consideration of S. 447, the Railroad Antimonopoly Act of 1985.

We further appreciate the opportunity of presenting these views at this time and respectfully ask that they be incorporated into and made part of the hearing record of your Committee on S. 447.

Sincerely yours,

Procompetitive Rail Steering Committee

By: ____________________________
M. E. Petruccelli
Vice-President

(Enclosures)

Attachment No.

PROCOMPETITIVE RAIL STEERING COMMITTEE

Section-by-Section Summary of Legislative Proposal

Introduction

When Congress enacted the Staggers Rail Act of 1980 it carefully balanced the interests of the railroads and the interests of the shipping public. The greater discretion accorded the railroads was in large part based upon the mandatory expectation that carrier competition, i.e., competition among and between the railroads themselves, would not only be preserved but would be strengthened. Such inter-railroad competition would ensure more efficient and more economical service for the shipping public.

However, as the Staggers Rail Act has been administered by the Interstate Commerce Commission, this objective of the Congress is not only not being achieved, it is being frustrated.

It is the belief of the Procompetitive Rail Steering Committee that clarifying legislation is necessary. It should be emphasized that this involves limited, additional action by the Congress to achieve the increased inter-railroad competition Congress originally had in mind in enacting the Staggers Rail Act.

The Procompetitive Rail Steering Committee's proposals are embodied in seven sections. A summary of the various proposals follows.

Section 1

This section designates the legislative proposal as the Railroad Competition Act of 1984.

Section 2

This section describes the proposal's purpose, which is to promote and strengthen competition between and among the nation's railroads in order fully to implement the present congressional railroad transportation policy.

Section 3

This section contains clarifying language directed to ensuring effective competition among rail carriers as well as between rail carriers and other modes.

Section 4

This section prohibits cancellation of through routes and/or joint rates where the purpose or effect of such actions is substantially to lessen competition, create a monopoly, or restrain trade. It permits aggrieved parties to obtain a permanent injunction from U.S. District Court against such railroad action, including rescission of any prohibited cancellation already in effect.

Section 5

This section is directed to enhancing inter-railroad competition, to achieve the objectives of the congressional rail transportation policy. Where a railroad provides service under a single line rate, or a joint line rate, on a particular category of traffic between a given origin and destination that railroad shall, upon request of another railroad having an actual or practicable interchange connection with the first railroad between the same origin and destination to do one of two things. It shall either participate in at least one competitive joint rail rate via that interchange on that traffic with that connecting rail carrier between the same points or it shall publish a competitive proportional rate on the traffic to or from that interchange point. This requirement shall apply at each actual or practicable interchange connection location. In addition to the carrier requesting the joint rate and through route any shipper or receiver desiring competitive rail service between the origin and destination also has standing to request and obtain comparable relief under the same conditions.

Section 6

This section makes mandatory rather than permissive the reciprocal switching provision contained in the Interstate Commerce Act where such agreements are practicable and in the public interest, or where necessary to provide alternate competitive rail service. This section also establishes time limits within which such agreements must be implemented. It prohibits cancellation of such agreements where the purpose is to eliminate competition or prevent alternate competitive rail service. Aggrieved parties have the right to obtain a permanent injunction against the cancellation or other obstruction from the U.S. District Court in the area in which the agreement has been, or would be, operative.

Section 7

This section makes mandatory the use of terminal facilities, including main line tracks for a reasonable distance beyond terminal areas, by carriers seeking to provide alternate competitive rail service if the ICC finds such use can be accomplished without impairing the ability of the rail carrier owning, or entitled to use, the facilities to handle its own business.

Section 8

This section requires that the Commission shall impose as a condition of approval of railroad merger applications that the carriers or their successors shall not cancel joint rates and/or through routes, or reciprocal switching agreements, or trackage rights agreements, in which they participate and they shall not refuse to participate in prospective joint rates or through routes, or reciprocal switching agreements, or trackage rights agreements, when or where the purpose or effect of such cancellation or refusal is the substantial lessening of competition between and among railroads, the creation of monopoly, or restraint of trade in railroad freight transportation.

Section 9

This section mandates that provisions of this legislative proposal apply to current or future railroad actions and retroactively to those occuring or consummated prior to the enactment of these provisions, including any segment of transportation which may otherwise have been exempted from regulation by the Interstate Commerce Commission under existing provisions of the Interstate Commerce Act.

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Attachment No.

PROCOMPETITIVE RAIL STEERING COMMITTEE

Legislative Proposal

A BILL

To amend Subtitle IV of title 49, United States Code, to promote and strengthen competition between and among the nation's railroads.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Short Title

Section 1. This Act may be cited as the "Railroad Competition Act of 1984."

Statement of Purpose

Section 2. The purpose of this Act is to promote and strengthen competition between and among the nation's railroads in order to implement fully the rail transportation policy in Section 10101a, Chapter 101, Subtitle IV, title 49, United States Code.

Rail Transportation Policy

Section 3. Subtitle IV, Chapter 101, title 49, United States Code, Section 10101a, sub-section (5) is amended to read:

(5) to foster sound economic conditions in transportation and to ensure effective competition and coordination both between and among rail carriers and between rail carriers and other modes.

Through Route/Joint Rate Cancellation

Section 4. Subtitle IV, Chapter 107, Subchapter I, title 49, United States Code, is amended by changing sub-sections (f), (g) and (h) of Section 10705 to read (h), (i), and (j), respectively, and by inserting a new sub-section (f) to read:

> (f) Notwithstanding all other provisions of Subtitle IV of this Title, cancellation by any rail carrier of any through route and/or joint rate where the purpose or effect has been, is, or will be the substantial lessening of competition between and among railroads, creation of monopoly, or restraint of trade in railroad freight transportation is prohibited. Any rail

carrier, shipper, receiver or other party adversely affected by such cancellation, actual or prospective, shall have the right to obtain a permanent injunction against such cancellation upon application to any district court of the United States located in the area in which the cancelling carrier provides or has provided rail transportation via such through route or under such joint rate. Such injunctive relief shall include rescission of any such cancellation which shall previously have become effective.

Establishment of Competitive Joint-or Proportional Rates

Section 5. Subtitle IV, Chapter 107, Subchapter I, title 49, United States Code, Section 10705, is amended by inserting after new sub-section (f) the following new sub-section (g):

(g) Notwithstanding all other provisions in this section, in order to achieve the objective of greater intramodal railroad competition any rail carrier providing service under a single line rate, or a joint line rate, on a particular category of traffic, between an origin and destination shall, upon request of a railroad having an actual or practicable interchange connection with said rail carrier between said origin and destination, either participate in at least one competitive joint rail rate via said interchange on such traffic with said connecting rail carrier between said points or shall publish a competitive proportional rate on such traffic to or from said interchange point. Said joint rate or proportional rate shall be conclusively deemed competitive if the ratio of revenue to variable costs realized from the division of the joint rate or from the proportional rate is no higher than that realized from the rail carrier's single line rate, or its division of said joint rate, between said origin and destination. Any shipper or receiver desiring competitive rail service between said origin and destination shall also have standing to request and obtain such alternative competitive railroad rate and service under the conditions above specified.

Reciprocal Switching

Section 6. Subtitle IV, Chapter 111, Subchapter I, title 49, United States Code, Section 11103(c) is amended by changing sub-section (c) (2) to sub-section (c) (3), by deleting sub-section (c) (1) and inserting the following:

(c) (1) Upon petition of any interested rail carrier, shipper, receiver or other party directly impacted, the Commission shall require rail carriers to enter into reciprocal switching agreements, where it finds such agreements to be practicable and in the public interest, or where such agreements are necessary to provide alternate competitive rail service. The Commission shall take final action upon such petition no later than one hundred twenty days after the filing of such petition with the Commission. The carriers entering into such an agreement shall establish the conditions and compensation applicable to such agreement in order to provide such alternate competitive rail service, but, if the carriers cannot agree upon such conditions and compensation within sixty days following service of the Commission's order requiring such agreement, the Commission shall, within sixty days thereafter, establish such conditions and compensation. Such compensation shall be limited to costs incurred plus a reasonable profit.

(c) (2) Cancellation of any reciprocal switching agreement, or obstruction of any prospective reciprocal switching agreement, the purpose or effect of which is to eliminate or to prevent alternate competitive rail service, is prohibited. Exaction of compensation for switching service in excess of costs incurred plus a reasonable profit shall be deemed constructive cancellation or obstruction and is prohibited. Any rail carrier, shipper, receiver or other party directly impacted by such cancellation or obstruction shall have the right to a permanent injunction against such cancellation or obstruction upon application to any district court of the United States in the area where such agreement is operative, or has been operative, or would be operative.

Use of Terminal Facilities

Section 7. Subtitle IV, Chapter 111, Subchapter 1, title 49, United States Code, Section 11103(a) is amended to read:

(a) Notwithstanding all other provisions of Subtitle IV of this Title, upon petition of any interested rail carrier, shipper, receiver or other party directly impacted, the Interstate Commerce Commission shall require terminal facilities, including mainline tracks, for a reasonable distance outside of a terminal, owned by a rail carrier providing transportation in interstate or foreign commerce, to be used by another rail carrier where necessary to provide alternate competitive rail service by the latter carrier if the Commission finds that use to be practicable without substantially impairing the ability of the rail carrier owning the facilities or entitled to use the facilities to handle its own business. The Commission shall take final action upon such petition no later than ninety days after the filing of such petition with the Commission. The carriers are responsible for establishing the conditions and compensation for the use of the facilities in order to provide such alternate competitive rail service. Such compensation shall be limited to costs incurred plus a reasonable profit. However, if the carriers cannot agree within sixty days following service of the Commission's order requiring such use, the Commission shall, within sixty days thereafter, establish conditions and compensation for use of the facilities. The compensation shall be paid or adequately secured before a carrier may begin to use the facilities of another carrier under this section.

Consolidation, Merger, and Acquisition of Control; General Procedures and Conditions of Approval

Section 8. Subtitle IV, Chapter 113, Subchapter III, title 49, United States Code, Section 11344(c) is amended to read:

(c) The Commission shall approve and authorize a transaction under this section when it finds the transaction is consistent with the public interest. The Commission, where one or more rail carriers are involved, shall impose as a condition of approval of the transaction that such carriers or successors thereof shall not cancel joint rates and/or through routes, or reciprocal switching agreements, or trackage rights agreements, in which such carriers participate, and shall not refuse to participate in prospective joint rates or through routes, or reciprocal switching agreements, or trackage rights agreements, when or where the purpose or effect of such cancellation or such refusal is the substantial lessening of competition between and among railroads, creation of monopoly, or restraint of trade in railroad freight transportation. The Commission may impose other conditions governing the transaction. When the transaction contemplates a guaranty or assumption of payment of dividends or of fixed-charges or will result in an increase of total fixed charges, the Commission may approve and authorize the transaction only if it finds the guaranty, assumption or increase is consistent with the public interest. When a rail carrier, or a person controlled by or affiliated with a rail carrier, is an applicant and the transaction involves a motor carrier, the Commission may approve and authorize the transaction only if it finds that the transaction is consistent with the public interest, will enable the rail carrier to use motor carrier transportation to public advantage in its operation, and will not unreasonably restrain competition. When a rail carrier is involved in the transaction, the Commission may require inclusion of other rail carriers located in the area involved in the transaction if they apply for inclusion and the Commission finds their inclusion to be consistent with the public interest.

Application

Section 9. Subtitle IV, Chapter 117, title 49, United States Code is amended by adding a new Section 11712 to read:

The provisions of sections 1 through 9 of this Act shall apply to current or future railroad actions and to those occurring or consummated prior to the enactment of these provisions, including those involving transportation in intrastate, interstate or foreign commerce which may otherwise have been exempted from regulation under subtitle IV of title 49, United States Code.

* * *

**PROCOMPETITIVE RAIL
STEERING COMMITTEE**

Suite 410, 1090 Vermont Avenue, NW
Washington, DC 20005
(202) 842-3870

March 6, 1986

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
SD-224 Dirksen Senate Office Building
Washington, D.C. 20510

Re: S. 447, The Railroad Antimonopoly
Act of 1986

Dear Mr. Chairman:

By our letter addressed to you on October 17, 1985 the Procompetitive Rail Steering Committee (PCRSC) expressed its interest in S. 447, The Railroad Antimonopoly Act of 1985. We indicated that we were actively engaged in studying and evaluating this proposed legislation and that, upon completion of this work, would further communicate our views to you and to your Committee.

The PCRSC has since carefully considered and discussed S. 447, including the revised draft dated November 12, 1985. We are aware of suggestions for further revision. In addition representatives of the PCRSC were present throughout the hearing on S. 447 held on March 4, 1986.

On behalf of the members of the Procompetitive Rail Steering Committee, listed in Appendix A, we wish to advise you of our basic support of S. 447, revised as of November 12, 1985. We shall appreciate it if this communication can be made part of the record of the hearing held on March 4, 1986.

The Procompetitive Committee urges early and favorable action by your Committee and the Senate upon this important piece of legislation.

Respectfully yours,

Michael E. Petruccelli
Vice President
Procompetitive Rail Steering Committee

cc: Members, Senate Committee on the Judiciary

APPENDIX A

List of Members of Procompetitive Rail Steering Committee Supporting S. 447

American Iron and Steel Institute
Amoco Chemicals Company
CF Industries, Inc.
Chrysler Corporation
Colt Industries, Inc.
FMC Corporation
ICI Americas, Inc.
International Paper Company
Libbey-Owens Ford Company
Manville Service Corporation
Monsanto Company
Nalco Chemical Company
Occidental Chemical Corporation
Olin Corporation
Owens-Illinois, Inc.
PPG Industries, Inc.
Reichhold Chemicals Inc.
Tennessee Eastman Company,
  Division of Eastman Kodak
Union Carbide Corporation
Wyandot Dolomite, Inc.

LaRoe, Winn & Moerman
ATTORNEYS AT LAW
EIGHTH FLOOR
1120 G STREET, N. W.
WASHINGTON, D.C. 20005
TELEPHONE (202) 628-2788
TELECOPIER (202) 628-2087
RCA TELEX 289603 LRWM UR

WILBUR LAROE, JR (1921-1957)
PAUL M DONOVAN
JOHN C KOLOJESKI
GERALD L RICHMAN
JEAN C GODWIN
STANLEY E HILTON
MICHAEL P WALLS°

SPECIAL COUNSEL
DAVID A SUTHERLUND
RAYMOND L POSTON, JR*°

*ALSO ADMITTED IN MD
°ALSO ADMITTED IN VA

MARYLAND OFFICE
17 W JEFFERSON STREET
SUITE 202
ROCKVILLE, MD 20850
(301) 251-9200

VIRGINIA OFFICE
313 PARK AVENUE
SUITE 400
FALLS CHURCH, VA 22046
(703) 237-0125

OF COUNSEL
ARTHUR L WINN, JR
SAMUEL H MOERMAN

March 17, 1986

Honorable Dennis DeConcini
United States Senate
328 Hart Senate Office Building
Washington, D.C. 20510

Re: *S. 447, The Railroad Antimonopoly Act.*

Dear Senator DeConcini:

At the March 4, 1986 hearings before the Senate Judiciary Committee, Federal Railroad Administrator John Riley expressed his opposition to the Railroad Antimonopoly Act. One of the objections raised by Mr. Riley was that the bill would be functionally impracticable because two railroads allegedly cannot operate over the same tracks. The purpose of this letter is to suggest that, contrary to Mr. Riley's opinion, it is a well-established practice within the industry for more than one carrier to operate over track segments. We discuss below just a few of the many instances where one rail carrier has been permitted to operate over another carrier's tracks purusant to a trackage rights arrangement.

1. In 1982, the Interstate Commerce Commission approved the merger of the Union Pacific and Missouri Pacific rail systems. *Union Pacific-Control-Missouri Pacific; Western Pacific*, 366 I.C.C. 462 (1982). In approving the merger, the Commission awarded substantial trackage rights to the following carriers: (a) the Denver & Rio Grande Western was granted 619 miles of trackage rights to operate over the Missouri Pacific system between Pueblo, Colorado and Kansas City, Missouri; (b) the Southern Pacific was granted 430 miles of trackage rights between Kansas City and St. Louis; and (c) the Missouri-Kansas-Texas was granted 195 miles of trackage rights between Kansas City and Omaha.

2. In 1980 the Commission approved CSX Corporation's application for control of the Chessie System and Seaboard System railroads. *CSX Corp.-Control-Chessie and Seaboard C.L.I.*, 363 I.C.C. 518 (1980), *petition for review denied*, 698 F.2d 315 (7th Cir. 1983). The Commission included in its decision the approval of 176 miles of trackage rights that the Chessie System had granted to the Norfolk & Western Railway to operate between Connellsville, Pennsylvania and Hagerstown, Maryland. The Delaware & Hudson Railway also obtained significant trackage rights in this proceeding.

3. The Delaware & Hudson operates over approximately 1700 miles of track. Of these 1700 miles, over 900 miles are owned by Conrail and operated over by the Delaware & Hudson pursuant to trackage rights awarded under the Final System Plan.

4. Conrail itself operates a substantial portion of its rail system pursuant to trackage rights agreements with other carriers. For example, Conrail operates along the Washington to Philadelphia, Harrisburg to Philadelphia and Hartford to New York corridors under trackage rights arrangements.

5. In December of 1981, the Baltimore & Ohio Railway Company ("B&O") agreed to lease over 89 miles of rail line that had been

abandoned by the bankrupt Rock Island railroad. The lease requires the B&O to grant overhead trackage rights to any rail carrier who operates any former Rock Island rail line contiguous to the trackage leased by the B&O. Pursuant to this lease provision, the Iowa Interstate Railroad has entered into a trackage rights arrangement with the B&O and operates over 75 miles of rail line between Joliet, Illinois and Bureau, Illinois.

6. In 1979 the Commission approved the Southern Pacific's operations over 196 miles of Missouri Pacific track between Harligen, Texas and Placedo, Texas. *Southern Pacific Transp. Co.-Abandonment*, 360 I.C.C. 138 (1979).

7. The Chicago & North Western and the Burlington Northern railroads both conduct operations over a 76 mile rail line in Wyoming's Powder River Basin that is jointly owned by the carriers. While technically not a trackage rights arrangement, the effect is the same in that two carriers are conducting operations over the same rail line.

8. In addition to sharing tracks with other carriers in the Powder River Basin, the Chicago & North Western also operates other portions of its system pursuant to trackage rights arrangements. For example, the C&NW has trackage rights along the Duluth, Minnesota to Minneapolis corridor as well as between Kansas City, Missouri and Leavenworth, Kansas.

9. Finally, I would also like to note that the feasibility of joint usage of rail tracks is apparent from the proposed acquisition of Conrail by Norfolk Southern. As Mr. Riley is well aware, the Norfolk Southern has entered into agreements with the Guilford System and the Pittsburgh & Lake Erie by which it would make hundreds of miles of its tracks available to Guilford and the P&LE pursuant to trackage rights arrangements.

The above are but a few of the many examples by which a railroad operates over another carrier's tracks pursuant to a trackage rights agreement. I hope this information has been helpful and would appreciate it if this letter can be included in the record of the March 4, 1986 hearing on S. 447. If I can be of further assistance, please do not hesitate to give me a call.

Very truly yours,

Paul M Donovan

Paul M. Donovan

PMD/jtc

UNION PACIFIC RAILROAD COMPANY

DREW LEWIS
CHAIRMAN

1416 DODGE STREET
OMAHA, NEBRASKA 68179

May 15, 1986

The Honorable Strom Thurmond
Chairman, Committee on the Judiciary
SD-224 Dirksen Senate Office Bldg.
Washington, D.C. 20510

Dear Mr. Chairman:

Union Pacific wishes to respond for the record to recent testimony before your Committee about rail transportation of soda ash. At the March 4th hearing on S. 447, the Railroad Antimonopoly Act, spokesmen for the Ad Hoc Committee on Soda Ash Transportation testified that Union Pacific and its connections are exercising market power to assess unreasonable rates for the transportation of Wyoming soda ash. Passage of S. 447, they contend, would rectify the situation by forcing the introduction of actual or simulated intramodal competition.

Union Pacific strongly opposes S. 447 and its counterpart in the House, HR 1140. We do not believe the record under the Staggers Act -- on soda ash or any other commodity -- shows a need for what is radical, and unprecedented rate regulation. Union Pacific's rates on soda ash are not unreasonable. Although Union Pacific is the only railroad serving soda ash shippers at Green River, Wyoming, the Railroad's rates are effectively constrained by intermodal, source and product competition.

We and the other carriers would be subject to a variety of conflicting restrictions because S. 447 would be interpreted differently by different courts. We would face difficulties in dealing with courts which have little experience considering all of the difficult and complex issues maximum rates and trackage rights involve. The proper forum for adjudication of these issues remains the Interstate Commerce Commission. We believe that, if enacted, S. 447 would lead to disinvestment in rail assets, jeopardize the safety of train operations and threaten the financial viability of existing railroads.

I have attached a paper for the Committee's consideration in its evaluation of S. 447 which explains in detail Union Pacific's rate actions on soda ash.

Very truly yours,

Drew

cc: The Honorable Joseph L. Biden, Jr

MAY 9, 1986

Response of Union Pacific Railroad to Allegations Made By the Ad Hoc Committee on Soda Ash Transportation

Summary

Rate Actions Under Staggers

- Since the Staggers Act became effective, Union Pacific's average revenue per ton on soda ash has increased 8% compared to cost increases of 21.4%. In 1983 and 1984, revenue per ton actually declined.

- Union Pacific has entered into 89 contracts involving the movement of soda ash.

- Special rates have been established to West Coast and Gulf ports to encourage exports.

Intermodal Competition

- Burlington Northern and the trucking firm Bonneville Transloaders, Inc. operate an intermodal operation for the movement of 300,000 tons of Wyoming soda ash annually. Soda ash is moved by truck from Green River to Bonneville, Wyoming and transloaded into BN hopper cars for delivery to destination. The operation is being expanded to handle 500,000 tons per year.

- Another operator is trucking 50,000 tons of soda ash per year to Ogden, Utah for subsequent rail movement by Southern Pacific or the D&RGW. Rio Grande has another transloading operation with a capacity of 100,000 tons in Salt Lake City. Nearly 10% of Green River soda ash is now being moved by truck for transloading. All of these operations are relatively new.

Product Competition

- Soda ash is used to manufacture glass and faces intense competition in the container market with substitutable paper, plastic and aluminum products. There is also competition from caustic soda and cullet which can reduce

- **Ogden Gateway. The Ogden gateway with Southern Pacific was closed due to the circuity of SP's route to the southern California market. Competition for soda ash shipments was not foreclosed since the real competition comes from the Searles Lake facility. In addition, there is a soda ash transloading operation through Ogden.**

Union Pacific Response to Allegations of Ad Hoc Committee on Soda Ash Transportation

On March 4, 1986, George Mauro, Director of Logistics for FMC Corporation, testified before the Senate Judiciary Committee in support of the Railroad Antimonopoly Act on behalf of the Ad Hoc Committee on Soda Ash Transportation. His support for the bill was predicated on alleged anti-competitive behavior and abuses of market power by Union Pacific Railroad (UP) and its connections.

The allegations of the Ad Hoc Committee on Soda Ash Transportation against UP and its connecting railroads fall into two categories. First, the Ad Hoc Committee claims the railroads, particularly UP, have virtually monopoly power and are assessing supra-competitive rates. Second, they charge the railroads have taken a number of anti-competitive actions to reduce competition.

Neither charge is true. There is substantial competition for the movement of soda ash that effectively restrains the rates railroads can charge. Actions claimed by the Ad Hoc Committee to be anti-competitive were undertaken to remove anomalies from the rate structure or to improve efficiency of rail operations.

Union Pacific Efforts to Encourage Development of the Wyoming Fields

Soda ash (sodium carbonate) is widely used in the manufacture of glass and as a sodium or alkali input in chemical processes. There are five natural producers located near Green River, Wyoming which is served by Union Pacific (UP) and a sixth at Searles Lake, California served by Southern Pacific (SP). In addition, Allied Chemical, one of the Wyoming producers, also operates a synthetic soda ash plant in Amherstburg, Ontario near Detroit. Nationwide, there are hundreds of soda ash receivers at more than 1500 destinations. The Ad Hoc Committee membership includes only three of the six producers and seven soda ash receivers. Ad Hoc Committee members receive soda ash at 121 destinations, or approximately 8% of the destinations to which UP and its connections have published rates.

Wyoming soda ash producers currently enjoy the lion's share of the soda ash market, due in part to the cooperative marketing efforts of the producers and Union Pacific. This has not always been the case. When FMC first began commercial production of soda ash in Wyoming in 1951, synthetic plants and Searles Lake, California refiners were the dominant suppliers.*/ Eleven synthetic plants in

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*/ FMC, the original Green River soda ash refiner commenced production in 1951. The others and the year they started production are: Stauffer Chemical Co., 1962; Allied Corporation, 1968; Texas Gulf Chemicals Co., 1976; and Tenneco Inc., 1982. That progress from no market share a few decades ago shows Union Pacific's rates have not hindered Green River production.

Michigan, Ontario, New York, Ohio, Virginia, Louisiana and Texas and two natural producers in Southern California had a major freight advantage over the Wyoming producers due to their proximity to receivers. Soda ash consumption was then and is now concentrated in the Northeast, industrial Midwest and southern California, hundreds of miles from Wyoming but relatively close to one or more then-competitors of the Wyoming producers. To enable FMC (and the other Wyoming producers as they began production) to penetrate the nation's markets, UP and its connections -- generally at the request of the Wyoming producers -- published a competitive rate schedule. This pricing strategy is known as a "missionary" rate structure.

Since the original "missionary" rates were published, the railroads have taken additional tariff reductions to meet competition at numerous destinations. Rates were reduced to several points in Eastern states in 1967 and 1971 to penetrate those markets and meet barge competition. Receivers in Illinois, Missouri and Kansas got a rate reduction in 1976. Sixty-eight points in Texas, Oklahoma, Louisiana and Arkansas obtained reduced rates in 1978 to meet a rate reduction by SP for California soda ash.

In addition to setting competitive rates for domestic traffic, UP has worked closely with the Wyoming producers to encourage exports to the Far East and Australia. Special rates have been established to West Coast and Gulf ports and UP is working with the American

Natural Soda Ash Corporation (ANSAC) to which all of the Wyoming producers belong, to encourage our respective trade representatives to negotiate for the abolition of barriers to importing U.S. soda ash in these counties. These efforts have met with some success as exports of Wyoming soda ash have increased.

Today's Soda Ash Charges Reflect the Existence of Competition

The original "missionary" rate structure is essentially the same one published today except for competitive adjustments.*/ The UP pricing strategy was successful in allowing the Wyoming producers to prosper. Since the establishment of the missionary rate structure, the synthetic plants have almost all closed and Wyoming's market share has gone from virtually nothing to 90 percent in January 1986, after a plant in New York closed.

Source Competition. Effective competition from other sources still exists. Kerr McGee Chemical Corporation at

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*/ The tariff reductions to numerous destinations were described above. In addition, the published rates have taken cost-based general rate increases approved by the ICC. Since the Staggers Act became law, the rates have taken the RCAF inflation increases permitted by 49 USC § 10707a. In addition, one general revenue enhancement increase of 5% was taken in October 1984. The Staggers Act permitted rail carriers to take revenue enhancement increases of up to 18% under 49 USC § 10707a(f), but market forces have prevented UP and its connections from taking full advantage of their statutory rights. The true compensatory level of these rates is discussed in more detail later.

Searles Lake, California has production capacity of 1,450,000 tons per year and can readily increase its production. Kerr McGee is the dominant supplier in California and also supplies the Mid-Atlantic area in rail-barge movement to its storage facility at Port Newark.[*] Allied Corporation, a Green River producer, also operates a synthetic plant at Amherstburg in Ontario. That plant has an annual capacity of 500,000 tons and is a mere 17 miles from Detroit and 76 miles from Toledo. Stauffer, a producer member of the Ad Hoc Committee, receives Amherstburg soda ash at its Chicago "Waterway" plant.

Another plant operated by Allied at Solvay, New York had a 33% market share in six Eastern states (which include 28 destinations of the Ad Hoc Committee members). Solvay had a capacity of 700,000 tons until it closed early this year. There has been no increase in rates to those Eastern points since Solvay's closing. Kerr McGee's presence in New Jersey and Burlington Northern's successful transloading operation from trucks at Bonneville, Wyoming have restrained UP's pricing freedom.

Intermodal Competition. Effective intermodal competition at origin is increasing. Burlington Northern (BN) in conjunction with Bonneville Transloading, Inc., a motor carrier, is moving approximately 300,000 tons per year from Green River to Bonneville, Wyoming where it is transloaded into BN covered hoppers for delivery to destination. This competitive alternative to UP is so successful its capacity is being expanded to 500,000 tons per year.*/ Bonneville is not the only successful soda ash transloading operation. There is a transloading operation run by Evans Grain with a capacity of 50,000 tons per year at Ogden, Utah which is served by SP and the Denver Rio Grande & Western. The Rio Grande has another transloading operation with a capacity of 100,000 tons in Salt Lake City. Altogether nearly 10% of the Green River soda ash is hauled by truck for transloading or direct delivery.

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[*] SP performs overland transportation to Texas City, Texas where the soda ash is transloaded into an ocean barge. Kerr McGee ships an estimated 100,000 tons per year to the East.

Product Competition. UP transportation of Wyoming soda ash faces indirect, but effective competition from soda ash substitutes and end product competition as well. Soda ash is used as a fluxing agent in the production of glass which constitutes half of the domestic use. The consumption of soda ash can be reduced 20% by the use of either caustic soda or cullet (recycled glass). Caustic soda and cullet are both widely available and reduce the energy needed in the manufacture of glass, making them attractive as partial substitutes for soda ash. If the delivered price of soda ash becomes too high, glass makers are able to increase their use of those alternatives to reduce their use of soda ash, which then reduces the movements of soda ash and railroad revenues. Caustic soda is fully substitutable for soda ash in many chemical manufacturing processes and is generally the preferred form of chlor-alkalai for chemical manufacturing.

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*/ The Ad Hoc Committee quotes an estimate that the joint truck-BN rates are as much as $500 to $1500 per carload below rates published by UP. While the Bonneville rates must be lower than Union Pacific's in order to attract traffic, the Ad Hoc Committee's estimate overstates the difference. As explained in more detail later, there is substantial discounting from the single-factor published rates from Green River by means of transportation service contracts.

A more intense form of product competition comes from paper, aluminum, and plastic containers which are rapidly taking market share from glass containers. If glass containers are unable to compete with non-glass containers on the basis of price, Union Pacific and its connections move less soda ash and have reduced revenues. Consequently, it is in the railroads' interest to see that the cost of glass containers is as competitive as possible with other forms of containers. Here too, the market place constrains the price which railroads can charge for transporting soda ash.

Union Pacific's Soda Ash Rates Are Reasonable.

The claims of the Ad Hoc Committee that its members are paying supra-competitive rates is simply not true.

Competitive forces set those rates originally and still constrain rail pricing. As the Interstate Commerce Commission recently found in Docket No. 38412S, Allied Chemical, et. al. v. Ann Arbor Railroad System, et. al. (the decision is on judicial review before the D.C. Circuit Court of Appeals) both geographic and product competition exist and are effective in restraining rail rates for the movement of Wyoming soda ash.*/ The effectiveness of competition in restraining rail rates is indicated by the prevalence of rate discounting as encouraged by the Staggers Act. As a result, the "missionary" tariff rate structure which was already competitively compelled acts as a price list from which significant discounts are being made by rail carriers across the country in response to market forces. Consequently, the published tariff rate seldom reflects the actual shipping charges paid.

The Ad Hoc Committee claims that rates challenged in the Allied complaint before the ICC were as high as 319 percent of revenue to variable cost and yielded before tax rates of return as high as 119.2 percent. This is inaccurate. Those numbers are derived from complainants' cost study which the Commission rejected.

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*/ All but two of the members of the Ad Hoc Committee (DeSoto and PPG) were complainants in the proceeding before the ICC, yet only 72 of the 121 destinations the members receive soda ash at were named in the complaint.

The Commission's cost findings determined the following distribution of revenue to variable cost ratios for the 241 routes costed in the case:

Below 160%	23
160.1% - 180%	65
180.1% - 225%	141
225.1% - 250%	8
250.1% - 275%	3
275.1% - 290%	1

Eighty-eight, or more than one-third, were found below the jurisdictional threshold of 180% established by Congress in 49 USC § 10709 (d)(2). Another 141 were found at or below 225%. Rates yielding ratios greater than 225% have been found below a reasonable maximum both before and after the Staggers Act by the ICC and upheld by the courts on judicial review.[*]

Moreover, the Commission's cost findings in Docket 38412 generally overstate the profitability of the complained-of rates since the record in *Allied Chemical* showed that as of 1983, 114 out of 157 complaint destinations had received the benefit of a rate discount by means of a contract.[*] Those discounts were as much as 21.8% of the published charge. Other railroads have published discounts in negative surcharge tariffs or charged a lower combination rate using a depressed rate and a contract as factors.[**] Through March, 1985 the Commission reported 485 transportation service contracts were filed providing either a refund or a new lower through or combination rate for soda ash movements. Union Pacific is a party to 36 contracts involving 36 different destinations with members of the Ad Hoc Committee and a total of 91 contracts to 75 destinations.

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[*] The Ad Hoc Committee has previously argued soda ash rates are excessive without success. For example, in evaluating a 1978 general rate increase, the ICC found soda ash rates generally ranged from 176 to 185 percent of variable cost and averaged 180.5%. It determined the proposed increase should be applied to soda ash since the range of ratios was not excessively high and soda ash would not contribute a disproportionate share of rail revenue. *Increased Rates and Charges, 1978 Nationwide*, 365 I.C.C. 14, 19 (1981).

UP is not privy to the terms of contracts of other railroads because they are confidential between the shipper and the contracting railroad. We have received reports from shippers that some railroads provide refunds ranging from

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[*] The highest ratio claimed was for a movement to an Ad Hoc Committee member at a destination which has moved under a contract rate since early 1983. UP granted the receiver a lower contract rate because the receiver had diverted 10% of its traffic to a motor carrier. That contract has been recently renewed with yet a lower rate in response to a threatened diversion to the Bonneville transload.

[**] A combination rate is a rate formed by combining two or more tariff or contract rates to form the total applicable rate from origin to destination. The individual rates which form the combination are "factors" in the rate. A combination rate "defeats" an otherwise applicable single-factor joint rate if it is lower. The shipper pays the lower applicable rate whether combination or single-factor.

$100 to $1,000 per carload or over $10 per ton on various movements. When all refunds, discounts and reductions for an entire movement are totalled, the through rate can be reduced by more than 20% on certain movements.

Some receivers reduce their transportation charges even further by using combination rates formed using particularly low published rates to destinations like Chicago, Chattanooga or Nashville and contract or published rates beyond. Under such arrangements UP's connecting carriers can protect their own revenue while reducing UP's earnings and offer a reduced rate to a shipper.[*] Such widespread and substantial discounting from published rates is inconsistent with the Ad Hoc Committee's claim of abuse of monopoly power.

Existing rates do not, as the Committee asserts, provide a rate of return exceeding 100% on a before tax basis. The Committee's calculation does not reflect the actual revenues received by the railroads for the movement since discounts are ignored. In addition, their figure is based only on an arbitrary allocation of system average variable costs and does not incorporate recovery of fixed costs which are at least twenty-five percent of total railroad costs.

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[*] Such combination rates and contracts offered by other carriers have reduced UP's revenue by more than $900 per carload on certain movements.

Nor does the perceived high cost of transporting soda ash relative to the price paid for the soda ash itself indicate the rates are high. It is unclear whether the 75% average claimed by the Ad Hoc Committee reflects the published rates or the actual rates paid. While it is true the cost of transporting Wyoming soda ash to reach its markets is a relatively high percentage of the delivered cost, that is caused by the distance of Wyoming from soda ash markets, not railroad market power. The very map the Ad Hoc Committee attached to its written statement shows the distance of the Wyoming producers from Committee members' destinations.*/

A more appropriate measure of the reasonableness of soda ash rates is to compare the revenue per ton/mile railroads earn on soda ash with that earned on other commodities. Soda ash revenue is lower than most other commodities originating in the Mountain Pacific Region (which includes Wyoming).

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*/ A copy of that same map with the location of the alternative sources of soda ash and transloading operations added is attached.

Mountain Pacific
To All Points In U.S.

Commodity		Cents Per Ton Mile
37	Transportation	9.25
41	Miscellaneous Freight	8.16
25	Furniture	7.86
35	Non Electric Machinery	6.78
39	Miscellaneous Mfd. Products	6.29
36	Electrical Machinery	5.75
30	Rubber and Plastics	5.66
34	Fabricated Metal Products	5.55
27	Printing Matter	5.25
29	Petroleum and Coal Products	5.10
49	Hazardous Materials	4.99
22	Textiles	4.81
44	Freight Forwarder	4.81
45	Shipper Association	4.81
10	Metallic Ores	4.26
19	Ordnance	4.07
42	Containers, Empty	4.07
40	Waste and Scrap	3.97
26	Pulp and Paper	3.84
32	Stone, Clay, or Glass Products	3.69
13	Crude Petroleum	3.46
33	Primary Metals	3.42
28	Chemicals	3.34
20	Foods	3.22
28-123	*Sodium Compounds incl. Soda Ash*	*3.18*
24	Wood Products	3.17
46	Miscellaneous Mixed Shipments	3.10
01	Farm Products	2.93
08	Forest Products	2.41
23	Apparel or Finished Textile Products	1.82
11	Coal	1.75

Source: 1982 Carload Waybill Statistics.

Soda ash is twenty-fifth out of 31 commodities. The raw materials which compete with soda ash in the production of containers, plastics (5.66¢), pulp and paper (3.84¢) and waste and scrap (which would include rail movements of cullet) (3.97¢), all yield higher revenue per ton mile.

Contrary to the Ad Hoc Committee's claims, soda ash shippers pay rates set by competitive forces and benefit from widespread discounting from the published tariff rates. The revenue per ton-mile paid to transport Wyoming soda ash compares favorably to other commodities. There is no evidence that UP or any other railroad has the ability to extract supra-competitive rates from shippers or receivers of Wyoming soda ash.

Individual Rate Actions/Gateway Closures

The Ad Hoc Committee also alleges UP and/or its connections have taken steps to eliminate or reduce the level of intramodal competition for Wyoming soda ash. Where those actions were challenged by shippers as being anticompetitive or unreasonable, the ICC has found they were justified and were not anticompetitive. A response to the detailed criticism follows.

Ann Arbor Rates. In order to attract more traffic to its inefficient and circuitous route which used a car ferry to cross Lake Michigan, the Ann Arbor Railroad System flagged out of the 7% general rate increase permitted by the ICC in Ex Parte No. 357 in 1978. Prior to its flagout, Ann Arbor did not handle a significant amount of soda ash traffic. The Ann Arbor flagout not only held down its revenues for each shipment, but also those of each other railroad in the joint rate. For example, over one routing UP received $460.64 less than over non-Ann Arbor routes to same destinations while Ann Arbor's division was cut only $58.90. This meant Union Pacific received $460.64 less on Ann Arbor routings although it provided transportation service identical to that for more direct routes. UP also had to provide more cars to the covered hopper pool at Green River to handle traffic because Ann Arbor routings increased turnaround time for the cars to return to origin by 12 days.

UP acquiesced in the Ann Arbor flagout for two years before taking defensive action. The delay was to see if the Ann Arbor strategy would increase total volume shipped and thereby offset the decreased revenue per shipment. When UP realized the Ann Arbor was not increasing overall tonnage but only cutting UP's revenue, UP finally acted to protect itself.

In 1981, Union Pacific published a notice cancelling its joint rates with the Ann Arbor but leaving the routes open. Combination rates over Ann Arbor routes were still available. The rate cancellation was suspended pending ICC investigation. While the ICC was still conducting the investigation and the Ann Arbor rates remained in effect, the Michigan Department of Transportation ended its subsidy of the Ann Arbor Railroad System and the Ann Arbor cross-lake operations ended. Thus, the loss of a subsidy -- not Union Pacific action -- ended the Ann Arbor flagout.*/

Gateways. For many years, a predecessor of Burlington Northern and Union Pacific maintained a gateway for the interchange of traffic in Grand Island, Nebraska. After the BN/Frisco merger, traffic via Grand Island was reduced to the point where retention of the gateway was no longer economical. In 1982 and 1983, Union Pacific closed that gateway with Burlington Northern on all through traffic for efficiency purposes. UP maintained larger and more efficient gateways with BN nearby at Kansas City and Omaha. UP has not eliminated Burlington Northern routes for eastbound soda ash traffic.

The Ogden gateway was a redundant and inefficient gateway to southern California since the SP route was circuitous. The closing of the Ogden gateway did not foreclose competition for soda ash shipments to California destinations. First, SP ships from a transloading operation capable of handling 50,000 tons a year through Ogden. Second, the real competition for soda ash traffic in California comes from soda ash from Searles Lake.*/

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*/ Ultimately when the Commission concluded its investigation, it found the cancellation was justified under long standing regulatory standards of efficiency and energy usage pursuant to 49 USC § 10705 (e), which permits the cancellation of inefficient routes. Joint Line Cancellation On Soda Ash By Union Pacific Railroad Company, 365 I.C.C. 951 (1982).

Selective Rate Increases. Union Pacific is also accused of increasing the rate to Denver to prevent its being used as a factor in establishing lower combination rates into the Southwest. Receivers at Denver ship under contract and are unaffected by the published rate. There was no traffic moving via the Denver rates to receivers in the Southwest. Receivers in that region already had the benefit of lower tariff rates reduced in 1978 in response to competition from Searles Lake.

St. Louis historically had depressed rates relative to nearby rates due to particularly intense source competition from Gulf Coast producers. When barge movements from those plants ended, the justification for maintaining the depressed St. Louis rate ended. UP corrected that rate anomaly by an increase to the "missionary" rate level which took effect January 10, 1980. At the instigation of some members of the Ad Hoc Committee and others, the Commission investigated the increase. It found that after the increase the revenue to variable cost ratio was 174.6%, which is below the current jurisdictional threshold. The Commission found the railroads proved the rate increase was justified and the rate was reasonable.

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*/ The Ad Hoc Committee also alleges the Seaboard, Illinois Central Gulf and Norfolk Southern have taken various anti-competitive actions. UP was not involved in those and is unable to comment on the motivation or justification for those actions. Those railroads, however, had entered into some 37 transportation service contracts for soda ash through March 30, 1985.

In 1983, a similar situation had arisen in connection with Chicago, Nashville and Chattanooga which also had depressed rates relative to other destinations. Those rates were being used as one factor in combination rates to defeat single factor rates to other destinations. This pricing strategy allowed UP connections to offer shippers a rate reduction by cutting UP's revenue. UP sought to eliminate the rate anomaly when it was no longer required to meet source competition at those points.

In order to minimize disruption to shippers, Union Pacific decided upon a phased-in increase over a three year period. One of the three scheduled increases to Nashville and Chattanooga took place as scheduled in 1983. That increase was not protested by members of the Ad Hoc Committee or any other shippers. Two of the proposed increases to Chicago took effect.*/ The rates to these three cities are still depressed relative to other points since the phased-in increases were not completed due to competition from the Bonneville transloading operation.

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*/ Only one of the Chicago increases was protested and then not on grounds the increase exceeded a reasonable maximum rate, but because of an alleged violation of rate bureau procedures.

If UP and its connections actually had substantial market power which they have used to thwart competition, as the Ad Hoc Committee has alleged, one would expect the railroads' revenue to increase more than their costs since the Staggers Act. But this is not the case. Since January 1, 1981, rail costs have increased over 21.4% as measured by the cumulative RCAF index. Yet UP's average revenue per ton of soda ash has increased only 7.97% from $26.45 to $28.56 in that same period. In fact, average UP revenue from soda ash declined in 1983 and 1984.*/ Such a decline in revenues is flatly inconsistent with the abuse of monopoly power claimed by the Ad Hoc Committee.

Summary

Most rate actions taken by Union Pacific or its connections on Wyoming rail soda ash rates have been procompetitive reductions in the published rate or contract and tariff discounts from the published rate in order to attract traffic. Overall Union Pacific's missionary pricing strategy has been successful for the railroads and has allowed the Wyoming producers to enjoy their current market share. As market conditions have changed, however, Union Pacific or its connections have sometimes taken steps affecting relatively few destinations to adjust. Overall, the rates for soda ash are still set by competitive market forces.

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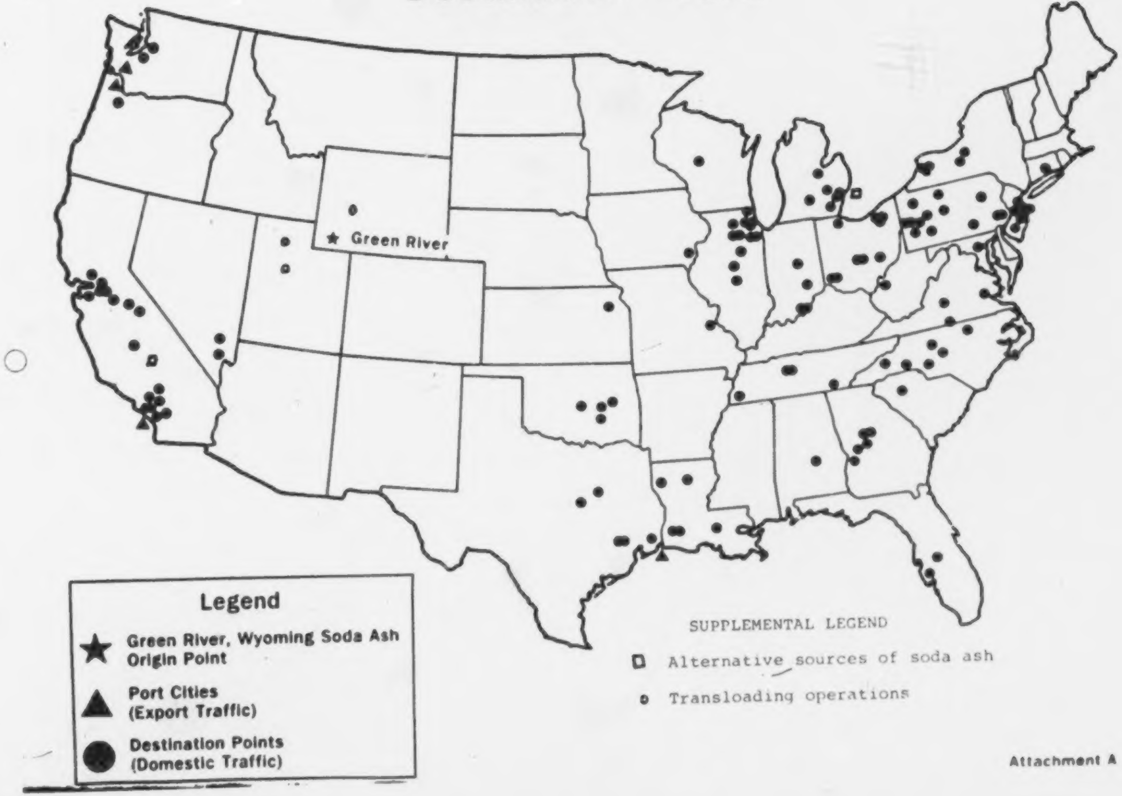
*/ That revenue decline occurred even though UP and its connections took a 5% revenue enhancement increase in 1984 after its earnings had eroded two years. It appeared the market could then absorb an increase designed to recoup a portion of prior reductions. The 1984 increase is the only non-cost based increase UP has taken on its overall soda ash traffic. Such an increase is moderate in view of the fact the Staggers Act allowed railroads to take revenue enhancement increases of up to 10 percent per year and up to 18% over a four year period under the zone of rate flexibility. 49 U.S.C. § 10707a.

Green River Soda Ash Destination Points


Green River
Legend
★ Green River, Wyoming Soda Ash Origin Point
▲ Port Cities (Export Traffic)
● Destination Points (Domestic Traffic)
SUPPLEMENTAL LEGEND
☐ Alternative sources of soda ash
○ Transloading operations

Attachment A